

AMENDED IN SENATE JUNE 20, 2005

AMENDED IN ASSEMBLY MAY 27, 2005

AMENDED IN ASSEMBLY MAY 2, 2005

CALIFORNIA LEGISLATURE—2005–06 REGULAR SESSION

ASSEMBLY BILL

No. 115

Introduced by Assembly Member Klehs

January 12, 2005

An act to amend Sections 17024.5, 17052.6, 17072, 17077, 17085, 17131, 17132.5, 17140, 17140.3, 17144, 17152, 17220, 17250, 17250.5, 17255, 17256, 17279.4, 17501, 17551, 17731, ~~18571, 18572, 18633, 19008, 19041.5, 19116, 19184, 19559, 17733, 18571, 18572, 18628, 18633, 18648, 19008, 19041.5, 19116, 19164, 19166, 19173, 19177, 19179, 19182, 19184, 19559, 23051.5, 23701s, 23701w, 23703.5, 23705, 23711, 23712, 24306, 24349, 24369.4, 24407, 24601, 24654, 24661.5, 24872, 24949.1, and 24949.3 of, to add Sections 17131.6, to amend and repeal Section 17204 of, to amend and repeal Sections 17204, 19772, 19774, and 19777 of, to add Sections 17131.6, 17139.6, 17201.4, 17201.5, 17201.6, 17204.7, 17681.6, ~~17760, 18035.6, 18036.6, 19136.7, 24355.3, 24406.6, 24661.6, 24694, 17734.6, 17760, 18035.6, 18036.6, 18181, 19136.12, 19164.5, 24355.3, 24355.4, 24406.6, 24661.6, 24694, and 24831.6 to, to add and repeal Sections 17053.62, 17255.5, 23662, and 24356.4 of, and to repeal Sections ~~17131.8, 17136.5, 17137, 17144.5, 17160.5, 17202.5, 17205, 19559, 19773, and 24356.5 of, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.~~~~~~

LEGISLATIVE COUNSEL'S DIGEST

AB 115, as amended, Klehs. Taxation: federal conformity.

Under the Personal Income Tax Law and the Corporation Tax Law, various provisions of the federal Internal Revenue Code, as enacted as of a specified date, are referenced in various sections of the Revenue and Taxation Code. Those laws provide that for taxable years beginning on or after January 1, 2002, the specified date of those referenced Internal Revenue Code sections is January 1, 2001, unless otherwise specifically provided.

Existing law requires, for any introduced bill that proposes changes in any of those dates, that the Franchise Tax Board prepare a complete analysis of the bill that describes all changes to state law that will automatically occur by reference to federal law as of the changed date. It further requires the Franchise Tax Board to immediately update and supplement that analysis upon any amendment to the bill, and requires that analysis to be made available to the public and to be submitted to the Legislature for publication in the daily journal of each house of the Legislature.

This bill would change the specified date of those referenced Internal Revenue Code sections to January 1, 2005, for taxable years beginning on or after January 1, 2005, and thereby would make numerous substantive changes to both the Personal Income Tax Law and the Corporation Tax Law with respect to those areas of preexisting conformity that are subject to changes under federal laws enacted after January 1, 2002, and that have not been, or are not being, excepted or modified.

This bill would make certain other changes in federal income tax laws applicable, with specified exceptions and modifications, and make specified supplemental, technical, or clarifying changes for purposes of the Personal Income Tax Law or the Corporation Tax Law, or both, with respect to, among other things, the exclusion from income of qualified foster care payments, health savings accounts, certain definitions, expensing for small businesses, low-income community tax credits, shareholder treatment, eligible shareholders, transfers of suspended losses incident to divorce, repayment of loans for qualifying employer securities, phaseouts of certain motor fuel excise taxes, suspension of occupational taxes relating to certain alcoholic beverages, information reporting for certain individuals, capital gain treatment applying to outright sales for landowners, expenses of rural letter carriers, expensing of certain reforestation expenditures, *depreciation of certain Alaskan pipeline property*, interest expense allocation rules, translation of foreign taxes, *certain*

passive foreign investment companies, Alaska Native Settlement trusts, civil rights tax relief, tax shelter provisions, underpayment penalty, and specified federal acts. This bill would specify various dates on which specified provisions apply, make findings and declarations that certain provisions are declaratory of existing law, and specify the intent and operation in the application of provisions conforming to various federal acts, and repeal obsolete provisions.

The Personal Income Tax Law and the Corporation Tax Law authorize various deductions and credits in computing the taxes imposed by those laws.

This bill would, under both laws, for taxable years beginning on or after ~~January 1, 2006~~ *July 1, 2005*, and before January 1, ~~2012~~ *2018*, allow an environmental tax credit in an amount equal to 5¢ for each gallon of ~~ultra-low~~ *ultra low* sulfur diesel fuel produced by a small refiner, as defined, at any facility located in this state.

This bill would also, under both laws, for a period beginning on January 1, 2005, and ending on January 1, 2009, authorize a small refiner to elect to treat 75% of qualified capital costs, as defined, as expenses not chargeable to a capital account and expenses that may be deducted, as provided.

This bill would take effect immediately as a tax levy.

The bill would provide that the operation of 2 of its sections would be contingent on the enactment of other specified bills.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

1 SECTION 1. Section 17024.5 of the Revenue and Taxation
2 Code is amended to read:
3 17024.5. (a) (1) Unless otherwise specifically provided, the
4 terms “Internal Revenue Code,” “Internal Revenue Code of
5 1954,” or “Internal Revenue Code of 1986,” for purposes of this
6 part, mean Title 26 of the United States Code, including all
7 amendments thereto as enacted on the specified date for the
8 applicable taxable year as follows:
9

| | | Specified Date of |
|----|---|-------------------|
| | | Internal Revenue |
| | Taxable Year | Code Sections |
| 1 | (A) For taxable years beginning on or after | |
| 2 | January 1, 1983, and on or before December | |
| 3 | 31, 1983..... | January 15, 1983 |
| 4 | (B) For taxable years beginning on or after | |
| 5 | January 1, 1984, and on or before December | |
| 6 | 31, 1984..... | January 1, 1984 |
| 7 | (C) For taxable years beginning on or after | |
| 8 | January 1, 1985, and on or before December | |
| 9 | 31, 1985..... | January 1, 1985 |
| 10 | (D) For taxable years beginning on or after | |
| 11 | January 1, 1986, and on or before December | |
| 12 | 31, 1986..... | January 1, 1986 |
| 13 | (E) For taxable years beginning on or after | |
| 14 | January 1, 1987, and on or before December | |
| 15 | 31, 1987..... | January 1, 1987 |
| 16 | (F) For taxable years beginning on or after | |
| 17 | January 1, 1989, and on or before December | |
| 18 | 31, 1989..... | January 1, 1989 |
| 19 | (G) For taxable years beginning on or after | |
| 20 | January 1, 1990, and on or before December | |
| 21 | 31, 1990..... | January 1, 1990 |
| 22 | (H) For taxable years beginning on or after | |
| 23 | January 1, 1991, and on or before December | |
| 24 | 31, 1991..... | January 1, 1991 |
| 25 | (I) For taxable years beginning on or after | |
| 26 | January 1, 1992, and on or before December | |
| 27 | 31, 1992..... | January 1, 1992 |
| 28 | (J) For taxable years beginning on or after | |
| 29 | January 1, 1993, and on or before December | |
| 30 | 31, 1993..... | January 1, 1993 |
| 31 | (K) For taxable years beginning on or after | |
| 32 | January 1, 1997, and on or before December | |
| 33 | 31, 1997 | January 1, 1997 |
| 34 | (L) For taxable years beginning on or after | |
| 35 | January 1, 1998, and on or before December | |
| 36 | 31, 2001 | January 1, 1998 |

(M) For taxable years beginning on or after
January 1, 2002, and on or before December 31,
2004..... January 1, 2001
(N) For taxable years beginning on or after
January 1, 2005..... January 1, 2005

(2) (A) Unless otherwise specifically provided, for federal laws enacted on or after January 1, 1987, and on or before the specified date for the taxable year, uncodified provisions that relate to provisions of the Internal Revenue Code that are incorporated for purposes of this part shall be applicable to the same taxable years as the incorporated provisions.

(B) In the case where Section 901 of the Economic Growth and Tax Relief Act of 2001 (Public Law 107-16) applies to any provision of the Internal Revenue Code that is incorporated for purposes of this part, Section 901 of the Economic Growth and Tax Relief Act of 2001 shall apply for purposes of this part in the same manner and to the same taxable years as it applies for federal income tax purposes.

(3) Subtitle G (Tax Technical Corrections) and Part I of Subtitle H (Repeal of Expired or Obsolete Provisions) of the Revenue Reconciliation Act of 1990 (Public Law 101-508) modified numerous provisions of the Internal Revenue Code and provisions of prior federal acts, some of which are incorporated by reference into this part. Unless otherwise provided, the provisions described in the preceding sentence, to the extent that they modify provisions that are incorporated into this part, are declaratory of existing law and shall be applied in the same manner and for the same periods as specified in the Revenue Reconciliation Act of 1990.

(b) Unless otherwise specifically provided, when applying any provision of the Internal Revenue Code for purposes of this part, a reference to any of the following is not applicable for purposes of this part:

(1) Except as provided in Chapter 4.5 (commencing with Section 23800) of Part 11 of Division 2, an electing small business corporation, as defined in Section 1361(b) of the Internal Revenue Code.

(2) Domestic international sales corporations (DISC), as defined in Section 992(a) of the Internal Revenue Code.

1 (3) A personal holding company, as defined in Section 542 of
2 the Internal Revenue Code.

3 (4) A foreign personal holding company, as defined in Section
4 552 of the Internal Revenue Code.

5 (5) A foreign investment company, as defined in Section
6 1246(b) of the Internal Revenue Code.

7 (6) A foreign trust, as defined in Section 679 of the Internal
8 Revenue Code.

9 (7) Foreign income taxes and foreign income tax credits.

10 (8) Section 911 of the Internal Revenue Code, relating to
11 United States citizens living abroad.

12 (9) A foreign corporation, except that Section 367 of the
13 Internal Revenue Code shall be applicable.

14 (10) Federal tax credits and carryovers of federal tax credits.

15 (11) Nonresident aliens.

16 (12) Deduction for personal exemptions, as provided in
17 Section 151 of the Internal Revenue Code.

18 (13) The tax on generation-skipping transfers imposed by
19 Section 2601 of the Internal Revenue Code.

20 (14) The tax, relating to estates, imposed by Section 2001 or
21 2101 of the Internal Revenue Code.

22 (c) (1) The provisions contained in Sections 41 to 44,
23 inclusive, and *Section* 172 of the Tax Reform Act of 1984
24 (Public Law 98-369), relating to treatment of debt instruments, is
25 not applicable for taxable years beginning before January 1,
26 1987.

27 (2) The provisions contained in Public Law 99-121, relating to
28 the treatment of debt instruments, is not applicable for taxable
29 years beginning before January 1, 1987.

30 (3) For each taxable year beginning on or after January 1,
31 1987, the provisions referred to by paragraphs (1) and (2) shall
32 be applicable for purposes of this part in the same manner and
33 with respect to the same obligations as the federal provisions,
34 except as otherwise provided in this part.

35 (d) When applying the Internal Revenue Code for purposes of
36 this part, regulations promulgated in final form or issued as
37 temporary regulations by “the secretary” shall be applicable as
38 regulations under this part to the extent that they do not conflict
39 with this part or with regulations issued by the Franchise Tax
40 Board.

1 (e) Whenever this part allows a taxpayer to make an election,
2 the following rules shall apply:

3 (1) A proper election filed with the Internal Revenue Service
4 in accordance with the Internal Revenue Code or regulations
5 issued by “the secretary” shall be deemed to be a proper election
6 for purposes of this part, unless otherwise provided in this part or
7 in regulations issued by the Franchise Tax Board.

8 (2) A copy of that election shall be furnished to the Franchise
9 Tax Board upon request.

10 (3) (A) Except as provided in subparagraph (B), in order to
11 obtain treatment other than that elected for federal purposes, a
12 separate election shall be filed at the time and in the manner
13 required by the Franchise Tax Board.

14 (B) (i) If a taxpayer makes a proper election for federal
15 income tax purposes prior to the time that taxpayer becomes
16 subject to the tax imposed under this part or Part 11
17 (commencing with Section 23001), that taxpayer is deemed to
18 have made the same election for purposes of the tax imposed by
19 this part, Part 10.2 (commencing with Section 18401), and Part
20 11 (commencing with Section 23001), as applicable, and that
21 taxpayer may not make a separate election for California tax
22 purposes unless that separate election is expressly authorized by
23 this part, Part 10.2 (commencing with Section 18401), or Part 11
24 (commencing with Section 23001), or by regulations issued by
25 the Franchise Tax Board.

26 (ii) If a taxpayer has not made a proper election for federal
27 income tax purposes prior to the time that taxpayer becomes
28 subject to tax under this part or Part 11 (commencing with
29 Section 23001), that taxpayer may not make a separate California
30 election for purposes of this part, Part 10.2 (commencing with
31 Section 18401), or Part 11 (commencing with Section 23001),
32 unless that separate election is expressly authorized by this part,
33 Part 10.2 (commencing with Section 18401), or Part 11
34 (commencing with Section 23001), or by regulations issued by
35 the Franchise Tax Board.

36 (iii) This subparagraph applies only to the extent that the
37 provisions of the Internal Revenue Code or the regulation issued
38 by “the secretary” authorizing an election for federal income tax
39 purposes apply for purposes of this part, Part 10.2 (commencing

1 with Section 18401) or Part 11 (commencing with Section
2 23001).

3 (f) Whenever this part allows or requires a taxpayer to file an
4 application or seek consent, the rules set forth in subdivision (e)
5 shall be applicable with respect to that application or consent.

6 (g) When applying the Internal Revenue Code for purposes of
7 determining the statute of limitations under this part, any
8 reference to a period of three years shall be modified to read four
9 years for purposes of this part.

10 (h) When applying, for purposes of this part, any section of the
11 Internal Revenue Code or any applicable regulation thereunder,
12 all of the following shall apply:

13 (1) References to “adjusted gross income” shall mean the
14 amount computed in accordance with Section 17072, except as
15 provided in paragraph (2).

16 (2) References to “adjusted gross income” for purposes of
17 computing limitations based upon adjusted gross income, shall
18 mean the amount required to be shown as adjusted gross income
19 on the federal tax return for the same taxable year.

20 (3) Any reference to “subtitle” or “chapter” shall mean this
21 part.

22 (4) The provisions of Section 7806 of the Internal Revenue
23 Code, relating to construction of title, shall apply.

24 (5) Any provision of the Internal Revenue Code that becomes
25 operative on or after the specified date for that taxable year shall
26 become operative on the same date for purposes of this part.

27 (6) Any provision of the Internal Revenue Code that becomes
28 inoperative on or after the specified date for that taxable year
29 shall become inoperative on the same date for purposes of this
30 part.

31 (7) Due account shall be made for differences in federal and
32 state terminology, effective dates, substitution of “Franchise Tax
33 Board” for “secretary” when appropriate, and other obvious
34 differences.

35 (i) Any reference to a specific provision of the Internal
36 Revenue Code shall include modifications of that provision, if
37 any, in this part.

38 SEC. 2. Section 17052.6 of the Revenue and Taxation Code
39 is amended to read:

17052.6. (a) For each taxable year beginning on or after January 1, 2000, there shall be allowed as a credit against the “net tax” (as defined in Section 17039) an amount determined in accordance with Section 21 of the Internal Revenue Code, except that the amount of the credit shall be a percentage, as provided in subdivision (b) of the allowable federal credit without taking into account whether there is a federal tax liability.

(b) For the purposes of subdivision (a), the percentage of the allowable federal credit shall be determined as follows:

(1) For taxable years beginning before January 1, 2003:

| If the adjusted gross income is: | The percentage of credit is: |
|---|------------------------------|
| \$40,000 or less..... | 63% |
| Over \$40,000 but not over \$70,000..... | 53% |
| Over \$70,000 but not over \$100,000..... | 42% |
| Over \$100,000..... | 0% |

(2) For taxable years beginning on or after January 1, 2003:

| If the adjusted gross income is: | The percentage of credit is: |
|---|------------------------------|
| \$40,000 or less..... | 50% |
| Over \$40,000 but not over \$70,000..... | 43% |
| Over \$70,000 but not over \$100,000..... | 34% |
| Over \$100,000..... | 0% |

(c) In the case of a taxpayer whose credits provided under this section exceed the taxpayer’s tax liability computed under this part, the excess shall be credited against other amounts due, if any, from the taxpayer and the balance, if any, shall be paid from the Tax Relief and Refund Account and refunded to the taxpayer.

(d) For purposes of this section, ~~adjusted gross income~~ “adjusted gross income” means adjusted gross income as computed for purposes of paragraph (2) of subdivision (h) of Section 17024.5.

(e) The credit authorized by this section shall be limited to employment-related expenses, within the meaning of Section 21 of the Internal Revenue Code, but only for child care services or care provided in this state and only to the extent of earned

1 income (within the meaning of Section 21(d) of the Internal
2 Revenue Code) from sources within this state.

3 (f) For purposes of this section, Section 21(b)(1) of the
4 Internal Revenue Code, relating to a qualifying individual, is
5 modified to additionally provide that a child (as defined in
6 Section 151(c)(3) of the Internal Revenue Code) shall be treated,
7 for purposes of Section 152 of the Internal Revenue Code (as
8 applicable for purposes of this section), as receiving over
9 one-half of his or her support during the calendar year from the
10 parent having custody for a greater portion of the calendar year,
11 that parent shall be treated as a “custodial parent” (within the
12 meaning of Section 152(e) of the Internal Revenue Code, as
13 applicable for purposes of this section), and the child shall be
14 treated as a qualifying individual under Section 21(b)(1) of the
15 Internal Revenue Code, as applicable for purposes of this section,
16 if both of the following apply:

17 (1) The child receives over one-half of his or her support
18 during the calendar year from his or her parents who never
19 married each other and who live apart at all times during the last
20 six months of the calendar year.

21 (2) The child is in the custody of one or both of his or her
22 parents for more than one-half of the calendar year.

23 (g) The amendments to this section made by the act adding
24 this subdivision shall apply only to taxable years beginning on or
25 after January 1, 2002.

26 *SEC. 2.5. Section 17052.6 of the Revenue and Taxation Code*
27 *is amended to read:*

28 17052.6. (a) For each taxable year beginning on or after
29 January 1, 2000, there shall be allowed as a credit against the
30 “net tax” (as defined in Section 17039) an amount determined in
31 accordance with Section 21 of the Internal Revenue Code, ~~as~~
32 ~~modified by the Economic Growth and Tax Relief Reconciliation~~
33 ~~Act of 2001 (Public Law 107-16)~~, except that the amount of the
34 credit shall be a percentage, as provided in subdivision (b) of the
35 allowable federal credit without taking into account whether
36 there is a federal tax liability.

37 (b) For the purposes of subdivision (a), the percentage of the
38 allowable federal credit shall be determined as follows:

39 (1) For taxable years beginning before January 1, 2003:

| | | |
|---|---|-------------------|
| 1 | | The percentage of |
| 2 | If the adjusted gross income is: | credit is: |
| 3 | \$40,000 or less..... | 63% |
| 4 | Over \$40,000 but not over \$70,000..... | 53% |
| 5 | Over \$70,000 but not over \$100,000..... | 42% |
| 6 | Over \$100,000..... | 0% |

(2) For taxable years beginning on or after January 1, 2003:

| | | |
|----|---|-------------------|
| 10 | | The percentage of |
| 11 | If the adjusted gross income is: | credit is: |
| 12 | \$40,000 or less..... | 50% |
| 13 | Over \$40,000 but not over \$70,000..... | 43% |
| 14 | Over \$70,000 but not over \$100,000..... | 34% |
| 15 | Over \$100,000..... | 0% |

(c) In the case of a taxpayer whose credits provided under this section exceed the taxpayer's tax liability computed under this part, the excess shall be credited against other amounts due, if any, from the taxpayer and the balance, if any, shall be paid from the Tax Relief and Refund Account and refunded to the taxpayer.

(d) For purposes of this section, adjusted gross income means adjusted gross income as computed for purposes of paragraph (2) of subdivision (h) of Section 17024.5.

(e) The credit authorized by this section shall be limited to employment-related expenses, as follows:

(1) *Employment-related expenses*, within the meaning of Section 21 of the Internal Revenue Code, ~~but only for child care shall be limited to expenses for household services or and care provided in this state and only to the extent of earned income (within the meaning of Section 21(d) of the Internal Revenue Code) from sources within this state.~~

(2) *Earned income*, within the meaning of Section 21(d) of the Internal Revenue Code, shall be limited to earned income subject to tax under this part. For purposes of this paragraph, compensation received by a member of the Armed Forces for active services as a member of the Armed Forces, other than pensions or retired pay, shall be considered earned income subject to tax under this part, whether or not the member is domiciled in this state.

(f) For purposes of this section, Section 21(b)(1) of the Internal Revenue Code, relating to a qualifying individual, is modified to additionally provide that a child (as defined in Section 151(c)(3) of the Internal Revenue Code) shall be treated, for purposes of Section 152 of the Internal Revenue Code (as applicable for purposes of this section), as receiving over one-half of his or her support during the calendar year from the parent having custody for a greater portion of the calendar year, that parent shall be treated as a “custodial parent” (within the meaning of Section 152(e) of the Internal Revenue Code, as applicable for purposes of this section), and the child shall be treated as a qualifying individual under Section 21(b)(1) of the Internal Revenue Code, as applicable for purposes of this section, if both of the following apply:

(1) The child receives over one-half of his or her support during the calendar year from his or her parents who never married each other and who live apart at all times during the last six months of the calendar year.

(2) The child is in the custody of one or both of his or her parents for more than one-half of the calendar year.

(g) The amendments to this section made by the act adding this subdivision shall apply only to taxable years beginning on or after January 1, 2002.

SEC. 3. Section 17053.62 is added to the Revenue and Taxation Code, to read:

17053.62. (a) For each taxable year beginning on or after ~~January 1, 2006, and before January 1, 2012~~ *July 1, 2005, and before January 1, 2018*, there shall be allowed as an environmental tax credit against the “net tax,” as defined by Section 17039, an amount equal to five cents (\$0.05) for each gallon of ~~ultra-low~~ *ultra low* sulfur diesel fuel produced during the taxable year by a small refiner at any facility located in this state.

(b) The aggregate credit determined under subdivision (a) for any taxable year with respect to any facility shall not exceed 25 percent of the qualified capital costs incurred by the small refiner with respect to that facility, reduced by the aggregate credits determined under this section for all prior taxable years with respect to that facility.

(c) For purposes of this section:

1 (1) “Small refiner” means any refiner who owns or operates a
2 refinery in California that:

3 (A) Has and at all times had since January 1, 1978, a crude oil
4 capacity of not more than 55,000 barrels per stream day.

5 (B) Has not been at any time since September 1, 1988, owned
6 or controlled by any refiner that at the same time owned or
7 controlled refineries in California with a total combined crude oil
8 capacity of more than 55,000 barrels per stream day.

9 (C) Has not been at any time since September 1, 1988, owned
10 or controlled by any refiner that at the same time owned or
11 controlled refineries in the United States with a total combined
12 crude oil capacity of more than 137,500 barrels per stream day.

13 (2) (A) “Qualified capital costs” means, with respect to any
14 facility, those costs paid or incurred during the applicable period
15 for items certified by the California Air Resources Board (*CARB*)
16 under subparagraph (B) for compliance with the applicable EPA
17 or *CARB* regulations with respect to that facility, including, but
18 not limited to, expenditures for the construction of new process
19 operation units or the dismantling and reconstruction of existing
20 process units to be used in the production of ~~ultra-low~~ *ultra low*
21 sulfur diesel fuel, associated adjacent or offsite equipment
22 (including tankage, catalyst, and power supply), engineering,
23 construction period interest, site work, and permitting.

24 (B) (i) Before claiming a credit under this section, a small
25 refiner shall request from the California Air Resources Board a
26 certification that both of the following are true:

27 (I) That the items for which qualified capital costs were paid
28 or incurred are for compliance with the applicable EPA or *CARB*
29 regulations described in subparagraph (A).

30 (II) That the items for which qualified capital costs were paid
31 or incurred have been placed in service by the small refiner.

32 (ii) The request described in clause (i) shall be in a form and
33 contain sufficient information to allow the California Air
34 Resources Board to determine that the items that are requested to
35 be certified were placed in service for compliance with
36 applicable EPA and *CARB* regulations, which information shall
37 include the date on which the items were placed in service.

38 (C) The California Air Resources Board shall make a
39 determination regarding a request described in subparagraph (B)
40 on or before 60 days after the request is submitted. If the board

1 does not make a determination within this time period, the
2 certification will be deemed to be granted.

3 *(D) If certification from the Secretary of the Treasury of the*
4 *United States, after consultation with the Administrator of the*
5 *Environmental Protection Agency, that the taxpayer's qualified*
6 *capital costs with respect to a facility are, or will result, in*
7 *compliance with applicable EPA regulations, has been received,*
8 *then the taxpayer shall be allowed the credit without obtaining*
9 *certification from the CARB, unless CARB demonstrates that the*
10 *fuel produced does not meet CARB regulations.*

11 (3) "Facility" means a small refiner's petroleum refinery
12 located in the State of California that has incurred qualified
13 capital costs to produce ~~ultra-low~~ ultra low sulfur diesel fuel.

14 (4) "Applicable EPA regulations" means the Highway Diesel
15 Fuel Sulfur Control Requirements of the Environmental
16 Protection Agency.

17 (5) "Applicable CARB regulations" means the Vehicular
18 Diesel Fuel Sulfur ~~(CARB) under Resolution 03-17. Control~~
19 *Requirements of the California Air Resources Board (CARB)*
20 *under Section 2281 of Article 2 of Chapter 5 of Division 3 of*
21 *Title 13 of the California Code of Regulations.*

22 (6) "Applicable period" means, with respect to any facility, the
23 period beginning on January 1, 2004, and ending on May 31,
24 2007.

25 (7) ~~"Ultra-low"~~ "Ultra low sulfur diesel fuel" means both of the
26 following:

27 (A) Diesel fuel with a sulfur content of 15 parts per million or
28 less.

29 (B) (i) Subject to clause (ii), either of the following:

30 (I) Vehicular diesel fuel produced and sold by a small refiner
31 on or after June 1, 2006.

32 (II) Vehicular diesel fuel produced and sold by the small
33 refiner before June 1, 2006, that the small refiner specifically
34 identifies and supports through internal test reports as meeting
35 applicable CARB regulations.

36 (ii) For purposes of this section, it is rebuttably presumed that
37 the fuel described in clause (i) is ~~ultra-low~~ ultra low sulfur diesel
38 fuel. The California Air Resources Board may rebut this
39 presumption by demonstrating that the fuel does not comply with
40 applicable CARB regulations.

1 (8) “Barrels per stream day” means the maximum number of
2 barrels of input that a distillation facility can process within a
3 24-hour period when running at full capacity under optimal crude
4 and product slate conditions with no allowance for downtime.

5 (d) For purposes of this section, if a credit is determined under
6 this section for any expenditure with respect to any property, the
7 increase in basis of that property that would (but for this
8 subdivision) result from that expenditure shall be reduced by the
9 amount of the credit so determined.

10 (e) No deduction shall be allowed for that portion of the
11 expenses otherwise allowable as a deduction for the taxable year
12 that is equal to the amount of the credit determined for the
13 taxable year under this section.

14 (f) In the case where the credit allowed by this section exceeds
15 the “net tax,” the excess may be carried over to reduce the “net
16 tax” in the following year, and the ~~six~~ 10 succeeding years if
17 necessary, until the credit is exhausted.

18 (g) If a small refiner that claims a credit under this section
19 sells, transfers, or otherwise disposes of, either directly or
20 indirectly, a facility within five years of the taxable year during
21 which it first claimed the credit, there shall be added to the “net
22 tax” of the small refiner during the taxable year of sale, transfer,
23 or disposition an amount equal to the total credit claimed
24 multiplied by a fraction, the numerator of which is the remaining
25 term of five years and the denominator of which is 5.

26 (h) This section is repealed on January 1, ~~2013~~ 2018.

27 SEC. 4. Section 17072 of the Revenue and Taxation Code is
28 amended to read:

29 17072. (a) Section 62 of the Internal Revenue Code, relating
30 to adjusted gross income defined, ~~applies~~ *shall apply*, except as
31 otherwise provided.

32 (b) Section 62(a)(2)(D) of the Internal Revenue Code, relating
33 to certain expenses of elementary and secondary school teachers,
34 shall not apply.

35 SEC. 5. Section 17077 of the Revenue and Taxation Code is
36 amended to read:

37 17077. Section 68 of the Internal Revenue Code, relating to
38 overall limitation on itemized deductions, shall apply, except as
39 otherwise provided.

1 (a) “Six percent” shall be substituted for “3 percent” in Section
2 68(a)(1) of the Internal Revenue Code.

3 (b) Section 68(b)(1) of the Internal Revenue Code shall not
4 apply and in lieu thereof the term “applicable amount” in each
5 place it appears in Section 68(a) of the Internal Revenue Code
6 means one hundred thousand dollars (\$100,000) in the case of a
7 single individual or a married individual ~~making filing~~ a separate
8 return, one hundred fifty thousand dollars (\$150,000) in the case
9 of a head of household, and two hundred thousand dollars
10 (\$200,000) in the case of a surviving spouse or a husband and
11 wife ~~making filing~~ a joint return.

12 (c) Section 68(b)(2) of the Internal Revenue Code, relating to
13 inflation adjustments, shall not apply. However, for any taxable
14 year beginning on or after January 1, 1992, the applicable
15 amounts specified in subdivision (b) shall be recomputed
16 annually in the same manner as the recomputation of income tax
17 brackets under subdivision (h) of Section 17041.

18 (d) Section 68(f) of the Internal Revenue Code, relating to
19 phaseout of limitation, shall not apply.

20 (e) Section 68(g) of the Internal Revenue Code, relating to
21 termination, shall not apply.

22 SEC. 6. Section 17085 of the Revenue and Taxation Code is
23 amended to read:

24 17085. Section 72 of the Internal Revenue Code, relating to
25 annuities and certain proceeds of life insurance contracts, is
26 modified as follows:

27 (a) The amendments and transitional rules made by Public
28 Law 99-514 shall be applicable to this part for the same
29 transactions and the same years as they are applicable for federal
30 purposes, except that the repeal of Section 72(d) of the Internal
31 Revenue Code, relating to repeal of special rule for employees’
32 annuities, shall apply only to the following:

33 (1) Any individual whose annuity starting date is after
34 December 31, 1986.

35 (2) At the election of the taxpayer, any individual whose
36 annuity starting date is after July 1, 1986, and before January 1,
37 1987.

38 (b) The amount of a distribution from an individual retirement
39 account or annuity or ~~employees’~~ ^{employee} trust or employee
40 annuity that is includable in gross income for federal purposes

1 shall be reduced for purposes of this part by the lesser of either of
2 the following:

3 (1) An amount equal to the amount includable in federal gross
4 income for the taxable year.

5 (2) An amount equal to the basis in the account or annuity
6 allowed by Section 17507 (relating to individual retirement
7 accounts and simplified employee pensions), the increased basis
8 allowed by Sections 17504 and 17506 (relating to plans of
9 self-employed individuals), the increased basis allowed by
10 Section 17501, or the increased basis allowed by Section 17551
11 that is remaining after adjustment for reductions in gross income
12 under this provision in prior taxable years.

13 (c) (1) Except as provided in paragraph (2), the amount of the
14 penalty imposed under this part shall be computed in accordance
15 with Sections 72(m), (q), (t), and (v) of the Internal Revenue
16 Code using a rate of 2½ percent, in lieu of the rate provided in
17 those sections.

18 (2) In the case where Section 72(t)(6) of the Internal Revenue
19 Code, relating to special rules for simple retirement accounts,
20 applies, the rate in paragraph (1) shall be 6 percent in lieu of the
21 2½ percent rate specified therein.

22 (d) Section 72(f)(2) of the Internal Revenue Code, relating to
23 special rules for computing employees' contributions, shall be
24 applicable without applying the exceptions which immediately
25 follow that paragraph.

26 SEC. 7. Section 17131 of the Revenue and Taxation Code is
27 amended to read:

28 17131. Part III of Subchapter B of Chapter 1 of Subtitle A of
29 the Internal Revenue Code, relating to items that are specifically
30 excluded from gross income, shall apply, except as otherwise
31 provided.

32 SEC. 8. Section 17131.6 is added to the Revenue and
33 Taxation Code, to read:

34 17131.6. Section 107 of the Internal Revenue Code is
35 modified by substituting in paragraph (2) the phrase "the rental
36 allowance paid to him or her as part of his or her compensation,
37 to the extent used by him or her to rent or provide a home" in lieu
38 of the phrase "the rental allowance paid to him as part of his
39 compensation, to the extent used by him to rent or provide a
40 home and to the extent such allowance does not exceed the fair

1 rental value of the home, including furnishings and
2 appurtenances such as a garage, plus the cost of utilities”
3 contained therein.

4 SEC. 9. Section 17131.8 of the Revenue and Taxation Code
5 is repealed.

6 SEC. 10. Section 17132.5 of the Revenue and Taxation Code
7 is amended to read:

8 17132.5. Section 101 of the Internal Revenue Code, relating
9 to certain death benefits, is modified as follows:

10 (a) Section 101(h) of the Internal Revenue Code, relating to
11 survivor benefits attributable to service by a public safety officer
12 who is killed in the line of duty, is modified to apply to amounts
13 received in taxable years beginning after December 31, 1996,
14 with respect to individuals dying after December 31, 1996.

15 (b) (1) Section 101 of the Internal Revenue Code, as modified
16 by subdivision (a) is modified to additionally provide that
17 Section 101(h) of the Internal Revenue Code shall not apply to
18 survivor benefits attributable to service by a public safety officer
19 who is killed in the line of duty with respect to deaths occurring
20 before December 31, 1996, that would otherwise be eligible for
21 exclusion pursuant to Section 101(h) of the Internal Revenue
22 Code, as modified by Public Law 107-15.

23 (2) The amendments made to this section by the act adding
24 this subdivision shall apply to amounts paid after December 31,
25 2001, with respect to deaths occurring on or before December 31,
26 1996.

27 (c) (1) Section 101 of the Internal Revenue Code, as modified
28 by subdivision (b), is modified to additionally provide that
29 Section 101(i) of the Internal Revenue Code shall apply to any
30 astronaut whose death occurs in the line of duty.

31 (2) The amendments made to this section by the act adding
32 this subdivision shall apply to amounts ~~paid~~ *received in taxable*
33 *years beginning* after December 31, 2002, with respect to deaths
34 occurring after that date.

35 SEC. 10.5. *Section 17136.5 of the Revenue and Taxation*
36 *Code is repealed.*

37 ~~17136.5. The provisions of Section 134(b)(3) of the Internal~~
38 ~~Revenue Code, relating to military benefits, as amended by~~
39 ~~Section 102 of the Military Family Tax Relief Act of 2003~~

1 ~~(Public Law 108-121), shall apply with respect to deaths~~
2 ~~occurring on or after September 11, 2001.~~

3 SEC. 11. Section 17137 of the Revenue and Taxation Code is
4 repealed.

5 SEC. 12. Section 17139.6 is added to the Revenue and
6 Taxation Code, to read:

7 17139.6. Section 139A of the Internal Revenue Code, relating
8 to federal subsidies for prescription drug plans, shall not apply.

9 SEC. 13. Section 17140 of the Revenue and Taxation Code is
10 amended to read:

11 17140. (a) For purposes of this section, the following terms
12 have the following meanings as provided in the Golden State
13 Scholarshare Trust Act (Article 19 (commencing with Section
14 69980) of Chapter 2 of Part 42 of the Education Code):

15 (1) "Beneficiary" has the meaning set forth in subdivision (c)
16 of Section 69980 of the Education Code.

17 (2) "Benefit" has the meaning set forth in subdivision (d) of
18 Section 69980 of the Education Code.

19 (3) "Participant" has the meaning set forth in subdivision (h)
20 of Section 69980 of the Education Code.

21 (4) "Participation agreement" has the meaning set forth in
22 subdivision (i) of Section 69980 of the Education Code.

23 (5) "Scholarshare trust" has the meaning set forth in
24 subdivision (f) of Section 69980 of the Education Code.

25 (b) For taxable years beginning *on or after January 1, 1998,*
26 *and* before January 1, 2002, except as otherwise provided in
27 subdivision (c), gross income of a beneficiary or a participant
28 does not include any of the following:

29 (1) Any distribution or earnings under a Scholarshare trust
30 participation agreement, as provided in Article 19 (commencing
31 with Section 69980) of Chapter 2 of Part 42 of the Education
32 Code.

33 (2) Any contribution to the Scholarshare trust on behalf of a
34 beneficiary shall not be includable as gross income of that
35 beneficiary.

36 (c) For taxable years beginning *on or after January 1, 1998,*
37 *and* before January 1, 2002:

38 (1) Any distribution under a Scholarshare trust participation
39 agreement shall be includable in the gross income of the
40 distributee in the manner as provided under Section 72 of the

1 Internal Revenue Code, as modified by Section 17085, to the
2 extent not excluded from gross income under this part. For
3 purposes of applying Section 72 of the Internal Revenue Code,
4 the following apply:

5 (A) All Scholarshare trust accounts of which an individual is a
6 beneficiary shall be treated as one account, except as otherwise
7 provided.

8 (B) All distributions during a taxable year shall be treated as
9 one distribution.

10 (C) The value of the participation agreement, income on the
11 participation agreement, and investment in the participation
12 agreement shall be computed as of the close of the calendar year
13 in which the taxable year begins.

14 (2) A contribution by a for-profit or nonprofit entity, or by a
15 state or local government agency, for the benefit of an owner or
16 employee of that entity or a beneficiary whom the owner or
17 employee has the power to designate, including the owner or
18 employee's minor children, shall be included in the gross income
19 of that owner or employee in the year the contribution is made.

20 (3) For purposes of this subdivision, "distribution" includes
21 any benefit furnished to a beneficiary under a participation
22 agreement, as provided in Article 19 (commencing with Section
23 69980) of Chapter 2 of Part 42 of the Education Code.

24 (4) (A) Paragraph (1) shall not apply to that portion of any
25 distribution that, within 60 days of distribution, is transferred to
26 the credit of another beneficiary under the Scholarshare trust who
27 is a "member of the family," as that term is used in Section
28 529(e)(2) of the Internal Revenue Code, as amended by Section
29 211 of the Taxpayer Relief Act of 1997 (P.L. 105-34), of the
30 former beneficiary of that Scholarshare trust.

31 (B) Any change in the beneficiary of an interest in the
32 Scholarshare trust shall not be treated as a distribution for
33 purposes of paragraph (1) if the new beneficiary is a "member of
34 the family," as that term is used in Section 529(e)(2) of the
35 Internal Revenue Code, as amended by Section 211 of the
36 Taxpayer Relief Act of 1997 (P.L. 105-34), of the former
37 beneficiary of that Scholarshare trust.

38 (d) For taxable years beginning on or after January 1, 2002,
39 Sections 529(c) and 529(e) of the Internal Revenue Code,
40 *relating to tax treatment of designated beneficiaries and*

1 *contributors and to other definitions and special rules,*
2 *respectively,* shall apply, except as otherwise provided in Part 11
3 (commencing with Section 23001) and this part.

4 SEC. 14. Section 17140.3 of the Revenue and Taxation Code
5 is amended to read:

6 17140.3. Section 529 of the Internal Revenue Code, relating
7 to qualified state tuition programs, shall apply, except as
8 otherwise provided.

9 (a) Section 529 (a) of the Internal Revenue Code is modified
10 as follows:

11 (1) By substituting the phrase “under this part and Part 11
12 (commencing with Section 23001)” in lieu of the phrase “under
13 this subtitle.”

14 (2) By substituting “Article 2 (commencing with Section
15 23731)” in lieu of “Section 511.”

16 (b) A copy of the report required to be filed with the Secretary
17 of the Treasury under Section 529(d) of the Internal Revenue
18 Code shall be filed with the Franchise Tax Board at the same
19 time and in the same manner as specified in that section.

20 SEC. 15. Section 17144 of the Revenue and Taxation Code is
21 amended to read:

22 17144. (a) Section 108(b)(2)(B) of the Internal Revenue
23 Code, relating to general business credit, is modified by
24 substituting “this part” in lieu of “Section 38 (relating to general
25 business credit).”

26 (b) Section 108(b)(2)(G) of the Internal Revenue Code,
27 relating to foreign tax credit carryovers, shall not apply.

28 (c) Section 108(b)(3)(B) of the Internal Revenue Code,
29 relating to credit carryover reduction, is modified by substituting
30 “11.1 cents” in lieu of “33 ⅓ cents” in each place in which it
31 appears. In the case where more than one credit is allowable
32 under this part, the credits shall be reduced on a pro rata basis.

33 (d) Section 108(g)(3)(B) of the Internal Revenue Code,
34 relating to adjusted tax attributes, is modified by substituting
35 “(\$9)” in lieu of “(\$3).”

36 (e) (1) If a taxpayer makes an election for federal income tax
37 purposes under Section 108(c) of the Internal Revenue Code,
38 relating to treatment of discharge of qualified real property
39 business indebtedness, a separate election shall not be allowed

1 under paragraph (3) of subdivision (e) of Section 17024.5 and the
2 federal election shall be binding for purposes of this part.

3 (2) If a taxpayer has not made an election for federal income
4 tax purposes under Section 108(c) of the Internal Revenue Code,
5 relating to treatment of discharge of qualified real property
6 business indebtedness, then the taxpayer shall not be allowed to
7 make that election for purposes of this part.

8 SEC. 16. Section 17144.5 of the Revenue and Taxation Code
9 is repealed.

10 SEC. 17. Section 17152 of the Revenue and Taxation Code is
11 amended to read:

12 17152. Section 121 of the Internal Revenue Code, relating to
13 exclusion of gain from sale of principal residence, is modified as
14 follows:

15 (a) The two-year period in Section 121(a) of the Internal
16 Revenue Code shall be reduced by the period of the taxpayer's
17 service, not to exceed 18 months, in the Peace Corps during the
18 five-year period ending on the date of the sale or exchange.

19 (b) If the taxpayer is prohibited from filing a joint return
20 pursuant to Section 18521, Section 121(b)(2)(A) of the Internal
21 Revenue Code shall nevertheless be treated as being satisfied if
22 the taxpayer files a joint return for federal income tax purposes
23 for the same taxable year. However, in no instance shall the total
24 amount excludable from gross income under Section 121(a) of
25 the Internal Revenue Code with respect to any sale or exchange
26 exceed the maximum amount allowed by Section 121(b) of the
27 Internal Revenue Code.

28 (c) (1) If a taxpayer has, at any time, made an election for
29 federal purposes under Section 121(f) of the Internal Revenue
30 Code not to have Section 121 of the Internal Revenue Code apply
31 to a sale or exchange, Section 121 of the Internal Revenue Code
32 shall not apply to that sale or exchange for state purposes, a
33 separate election for state purposes shall not be allowed under
34 paragraph (3) of subdivision (e) of Section 17024.5, the federal
35 election shall be binding for purposes of this part, and that
36 election shall be treated as an election to include in gross income
37 for purposes of this part all the gain from the sale or exchange of
38 that property, including that amount which, but for that election,
39 would have been excluded from income under Section 121(a) of
40 the Internal Revenue Code for state purposes.

(2) If a taxpayer fails to make an election for federal purposes under Section 121(f) of the Internal Revenue Code to not have Section 121 of the Internal Revenue Code apply to a sale or exchange, no election under Section 121(f) of the Internal Revenue Code shall be allowed for state purposes, Section 121 of the Internal Revenue Code shall apply to that sale or exchange for state purposes, and a separate election for state purposes shall not be allowed under paragraph (3) of subdivision (e) of Section 17024.5.

(d) (1) If a taxpayer has, at any time, made an election for federal purposes under Section 312(d)(2) of the Taxpayer Relief Act of 1997 (Public Law 105-34), relating to sales before date of enactment, or Section 312(d)(4) of that act, relating to binding contracts, to not have the amendments made by Section 312 of the Taxpayer Relief Act of 1997 (Public Law 105-34) apply to a sale or exchange, the amendments made by the act adding this subdivision shall not apply to that sale or exchange, Sections 1, 4, and 6 of Chapter 610 of the Statutes of 1997 shall not apply to that sale or exchange, a separate election for state purposes shall not be allowed under paragraph (3) of subdivision (e) of Section 17024.5, and the federal election shall be binding for purposes of this part.

(2) If a taxpayer fails to make an election for federal purposes under Section 312(d)(2) of the Taxpayer Relief Act of 1997 (Public Law 105-34), relating to sales before date of enactment, or Section 312(d)(4) of that act, relating to binding contracts, to not have the amendments made by Section 312 of the Taxpayer Relief Act of 1997 (Public Law 105-34) apply to a sale or exchange, an election under Section 312(d)(2) of the Taxpayer Relief Act of 1997 (Public Law 105-34), relating to sales before date of enactment, or Section 312(d)(4) of that act, relating to binding contracts, shall not be allowed for state purposes, the amendments made by the act adding this subdivision shall apply to that sale or exchange, Sections 1, 4, and 6 of Chapter 610 of the Statutes of 1997 shall apply to that sale or exchange, and a separate election for state purposes shall not be allowed under paragraph (3) of subdivision (e) of Section 17024.5.

(e) (1) If a taxpayer has, at any time, made or revoked an election for federal purposes under Section 121(d)(9) of the Internal Revenue Code to suspend the running of the five-year

1 period described in Sections 121(a), 121(c)(1)(B), and 121(d)(7)
2 of the Internal Revenue Code, that election or revocation of
3 election to suspend the five-year period under Section 121(d)(9)
4 of the Internal Revenue Code shall be applicable for state
5 purposes, a separate election or revocation of election for
6 purposes of Section 121(d)(9) of the Internal Revenue Code may
7 not be allowed under paragraph (3) of subdivision (e) of Section
8 17024.5, and the federal election or revocation of election shall
9 be binding for purposes of this part.

10 (2) If a taxpayer fails to make an election for federal purposes
11 under Section 121(d)(9) of the Internal Revenue Code to suspend
12 the running of the five-year period described in Sections 121(a),
13 121(c)(1)(B), and 121(d)(7) of the Internal Revenue Code, that
14 five-year period may not be suspended under Section 121(d)(9)
15 of the Internal Revenue Code for state purposes, and a separate
16 election for state purposes shall not be allowed under paragraph
17 (3) of subdivision (e) of Section 17024.5.

18 (f) Section 121(d)(10) of the Internal Revenue Code, relating
19 to property acquired from a decedent, shall not apply.

20 SEC. 18. Section 17160.5 of the Revenue and Taxation Code
21 is repealed.

22 SEC. 19. Section 17201.4 is added to the Revenue and
23 Taxation Code, to read:

24 17201.4. Section 179B of the Internal Revenue Code, relating
25 to deductions for capital costs incurred in complying with
26 Environmental Protection Agency sulfur regulations, shall not
27 apply.

28 SEC. 20. Section 17201.5 is added to the Revenue and
29 Taxation Code, to read:

30 17201.5. Section 181 of the Internal Revenue Code, relating
31 to treatment of certain qualified film and television productions,
32 shall not apply.

33 SEC. 21. Section 17201.6 is added to the Revenue and
34 Taxation Code, to read:

35 17201.6. Section 199 of the Internal Revenue Code, relating
36 to income attributable to domestic production activities, shall not
37 apply.

38 SEC. 22. Section 17202.5 of the Revenue and Taxation Code
39 is repealed.

1 SEC. 23. Section 17204 of the Revenue and Taxation Code is
2 amended to read:

3 17204. (a) Section 221 of the Internal Revenue Code,
4 relating to interest on education loans, is modified to additionally
5 provide that a deduction shall be allowed under this section only
6 with respect to interest paid on any qualified education loan
7 during the first 60 months, whether or not consecutive, in which
8 interest payments are required. For purposes of this subdivision,
9 any loan and period shall be determined in the form and manner
10 prescribed in forms and instructions by the Franchise Tax Board
11 in the case of multiple loans that are refinanced by, or serviced
12 as, a single loan and in the case of loans incurred before January
13 1, 2005.

14 (b) (1) Section 221(b)(2)(B)(i)(I) of the Internal Revenue
15 Code is modified by ~~substitution~~ *substituting* the phrase “\$40,000
16 (\$60,000 in the case of a joint return)” in lieu of the phrase
17 “\$50,000 (\$100,000 in the case of a joint return)” contained
18 therein.

19 (2) Section 221(b)(2)(B)(ii) of the Internal Revenue Code is
20 modified by substituting the phrase “\$15,000” in lieu of the
21 phrase “\$15,000 (\$30,000 in the case of a joint return)” contained
22 therein.

23 (3) Section 221(f)(1) of the Internal Revenue Code is modified
24 by substituting the phrase “\$40,000 and \$60,000 amounts” in lieu
25 of the phrase “\$50,000 and \$100,000 amounts” contained therein.

26 (c) This section shall apply to taxable years beginning on and
27 after January 1, 2005, and before January 1, 2007. This section
28 shall remain in effect only until January 1, 2007, and as of that
29 date is repealed.

30 SEC. 24. Section 17204.7 is added to the Revenue and
31 Taxation Code, to read:

32 17204.7. Section 222 of the Internal Revenue Code, relating
33 to qualified tuition and related expenses, shall not apply.

34 SEC. 25. Section 17205 of the Revenue and Taxation Code,
35 as added by Section 14 of Chapter 34 of the Statutes of 2002, is
36 repealed.

37 SEC. 26. Section 17205 of the Revenue and Taxation Code,
38 as added by Section 14 of Chapter 35 of the Statutes of 2002, is
39 repealed.

SEC. 27. Section 17220 of the Revenue and Taxation Code is amended to read:

17220. (a) Section 164(a)(3) of the Internal Revenue Code, relating to the deductibility of state, local, and foreign income, war profits, and excess profits taxes, shall not apply.

(b) Section 164(b)(5) of the Internal Revenue Code, relating to general sales taxes, shall not apply.

(c) In addition to the provisions of Section 164(c) of the Internal Revenue Code, relating to deduction denied in case of certain taxes, no deduction shall be allowed for any tax imposed under Chapter 10.5 (commencing with Section 17935), Chapter 10.6 (commencing with Section 17941), or Chapter 10.7 (commencing with Section 17951) of this part or under Part 11 (commencing with Section 23001).

SEC. 28. Section 17250 of the Revenue and Taxation Code is amended to read:

17250. (a) Section 168 of the Internal Revenue Code is modified as follows:

(1) Any reference to “tax imposed by this chapter” in Section 168 of the Internal Revenue Code means “net tax,” as defined in Section 17039.

(2) (A) Section 168(e)(3) is modified to provide that any grapevine, replaced in a vineyard in California in any taxable year beginning on or after January 1, 1992, as a direct result of a phylloxera infestation in that vineyard, or replaced in a vineyard in California in any taxable year beginning on or after January 1, 1997, as a direct result of Pierce’s Disease in that vineyard, shall be “five-year property,” rather than “10-year property.”

(B) Section 168(g)(3) of the Internal Revenue Code is modified to provide that any grapevine, replaced in a vineyard in California in any taxable year beginning on or after January 1, 1992, as a direct result of a phylloxera infestation in that vineyard, or replaced in a vineyard in California in any taxable year beginning on or after January 1, 1997, as a direct result of Pierce’s Disease in that vineyard, shall have a class life of 10 years.

(C) Every taxpayer claiming a depreciation deduction with respect to grapevines as described in this paragraph shall obtain a written certification from an independent state-certified integrated pest management adviser, or a state agricultural

1 commissioner or adviser, that specifies that the replanting was
2 necessary to restore a vineyard infested with phylloxera or
3 Pierce's Disease. The taxpayer shall retain the certification for
4 future audit purposes.

5 (3) Section 168(j) of the Internal Revenue Code, relating to
6 property on Indian reservations, shall not apply.

7 (4) Section 168(k) of the Internal Revenue Code, *relating to*
8 *special allowance for certain property acquired after September*
9 *10, 2001, and before January 1, 2005*, shall not apply.

10 (5) Sections 168(b)(3)(G) and 168(b)(3)(H) of the Internal
11 Revenue Code, *relating to property to which the straight line*
12 *method applies*, shall not apply.

13 (6) Sections 168(e)(3)(E)(iv) and 168(e)(3)(E)(v) of the
14 Internal Revenue Code, *relating to 15-year property*, shall not
15 apply.

16 (7) Sections 168(e)(6) and 168(e)(7) of the Internal Revenue
17 Code, *relating to qualified leasehold improvement property and*
18 *to qualified restaurant property, respectively*, shall not apply.

19 (b) Section 169 of the Internal Revenue Code, relating to
20 amortization of pollution control facilities, is modified as
21 follows:

22 (1) The deduction allowed by Section 169 of the Internal
23 Revenue Code shall be allowed only with respect to facilities
24 located in this state.

25 (2) The "state certifying authority," as defined in Section
26 169(d)(2) of the Internal Revenue Code, means the State Air
27 Resources Board, in the case of air pollution, and the State Water
28 Resources Control Board, in the case of water pollution.

29 SEC. 29. Section 17250.5 of the Revenue and Taxation Code
30 is amended to read:

31 17250.5. Section 167(g) of the Internal Revenue Code,
32 relating to depreciation under income forecast method, shall be
33 modified as follows:

34 (a) Section 167(g)(2)(C) of the Internal Revenue Code is
35 modified by substituting "Section 19521" in lieu of "Section
36 460(b)(7)" of the Internal Revenue Code.

37 (b) Section 167(g)(5)(D) of the Internal Revenue Code is
38 modified by substituting "Part 10.2 (commencing with Section
39 18401) (other than Section 19136)" in lieu of "Subtitle F (other
40 than Sections 6654 and ~~6655~~: 6655)." "

1 (c) Section 167(g)(5)(E) of the Internal Revenue Code,
2 *relating to treatment of distribution costs*, shall not apply.

3 (d) Section 167(g)(7) of the Internal Revenue Code, *relating to*
4 *treatment of participations and residuals*, shall not apply.

5 SEC. 30. Section 17255 of the Revenue and Taxation Code is
6 amended to read:

7 17255. (a) Section 179(b)(1) of the Internal Revenue Code,
8 relating to dollar limitation, shall not apply and in lieu thereof,
9 the aggregate cost which may be taken into account under
10 Section 179(a) of the Internal Revenue Code for any taxable year
11 shall not exceed twenty-five thousand dollars (\$25,000).

12 (b) Section 179(b)(2) of the Internal Revenue Code, relating to
13 reduction in limitation, shall not apply and in lieu thereof, the
14 limitation under subdivision (a) for any taxable year shall be
15 reduced, but not to below zero, by the amount by which the cost
16 of Section 179 property, as defined in Section 179(d)(1) of the
17 Internal Revenue Code, except as otherwise provided, placed in
18 service during the taxable year exceeds two hundred thousand
19 dollars (\$200,000).

20 (c) Section 179 of the Internal Revenue Code is modified to
21 provide that the “aggregate amount disallowed” referred to in
22 Section 179(b)(3)(B) of the Internal Revenue Code shall be
23 computed under this part as it read on the date the property
24 generating the amount disallowed was placed in service.

25 (d) Section 179(b)(5) of the Internal Revenue Code, relating to
26 inflation adjustments, shall not apply.

27 (e) The last sentence in Section 179(c)(2) of the Internal
28 Revenue Code, relating to election irrevocable, shall not apply.

29 (f) Section 179(d)(1)(A)(ii) of the Internal Revenue Code,
30 relating to computer software, shall not apply.

31 SEC. 31. Section 17255.5 is added to the Revenue and
32 Taxation Code, to read:

33 17255.5. (a) ~~For any taxable year which includes part of~~
34 ~~the “applicable period” as defined in paragraph (6) of~~
35 ~~subdivision (c) of Section 17053.62, a small refiner (as defined in~~
36 ~~Section 17053.62) may elect to treat 75 percent of qualified~~
37 ~~capital costs (as defined in paragraph (2) of subdivision (c) of~~
38 ~~Section 17053.62) for items that are placed in service paid or~~
39 ~~incurred~~ by the taxpayer during the taxable year as expenses that
40 are not chargeable to capital account. Any cost so treated shall be

1 allowed as a deduction for the taxable year in which paid or
2 incurred.

3 (b) (1) For purposes of this part, the basis of any property
4 shall be reduced by the portion of the cost of that property taken
5 into account under subdivision (a).

6 (2) For purposes of Section 1245 of the Internal Revenue
7 Code, and corresponding section of this code, the amount of the
8 deduction allowable under subdivision (a) with respect to any
9 property which is of a character subject to the allowance for
10 depreciation shall be treated as a deduction allowed for
11 depreciation under Section 167 of the Internal Revenue Code, or
12 the corresponding section of this code.

13 (c) This section shall remain in effect only until January 1,
14 2009, and as of that date is repealed.

15 SEC. 32. Section 17256 of the Revenue and Taxation Code is
16 amended to read:

17 17256. Section 179A of the Internal Revenue Code, relating
18 to deduction for clean-fuel vehicles and certain refueling
19 property, shall not apply.

20 SEC. 33. Section 17279.4 of the Revenue and Taxation Code
21 is amended to read:

22 17279.4. Section 198 of the Internal Revenue Code, relating
23 to expensing of environmental remediation costs, is modified as
24 follows:

25 (a) For expenditures paid or incurred before January 1, 2004,
26 all of the following shall apply:

27 (1) If a taxpayer has, at any time, made an election for federal
28 purposes under Section 198(a) of the Internal Revenue Code to
29 have Section 198 of the Internal Revenue Code apply to a
30 qualified environmental remediation expenditure, Section 198 of
31 the Internal Revenue Code shall apply to that qualified
32 environmental remediation expenditure for state purposes, a
33 separate election for state purposes shall not be allowed under
34 paragraph (3) of subdivision (e) of Section 17024.5, and the
35 federal election shall be binding for purposes of this part.

36 (2) If a taxpayer fails to make an election for federal purposes
37 under Section 198(a) of the Internal Revenue Code to have
38 Section 198 of the Internal Revenue Code apply to a qualified
39 environmental remediation expenditure, an election under
40 Section 198(a) of the Internal Revenue Code shall not be allowed

1 for state purposes, Section 198 of the Internal Revenue Code
2 shall not apply to that qualified environmental remediation
3 expenditure for state purposes, and a separate election for state
4 purposes shall not be allowed under paragraph (3) of subdivision
5 (e) of Section 17024.5.

6 (b) No inference as to the proper treatment for purposes of this
7 part of qualified environmental remediation expenditures ~~for~~
8 ~~periods before the enactment of this section~~ paid or incurred in
9 taxable years beginning before January 1, 1998, shall be made.

10 (c) Section 198(h) of the Internal Revenue Code *relating to*
11 *termination*, shall not apply.

12 (d) Section 198 of the Internal Revenue Code, *relating to*
13 *expensing of environmental remediation costs*, shall not apply to
14 expenditures paid or incurred after December 31, 2003.

15 SEC. 34. Section 17501 of the Revenue and Taxation Code is
16 amended to read:

17 17501. (a) Subchapter D of Chapter 1 of Subtitle A of the
18 Internal Revenue Code, relating to deferred compensation, shall
19 apply, except as otherwise provided.

20 (b) Notwithstanding the specified date contained in paragraph
21 (1) of subdivision (a) of Section 17024.5, Part I of Subchapter D
22 of Chapter 1 of Subtitle A of the Internal Revenue Code, relating
23 to pension, profitsharing, stock bonus plans, etc., shall apply,
24 except as otherwise provided, without regard to taxable year to
25 the same extent as applicable for federal income tax purposes.

26 (c) The maximum amount of elective deferrals (as defined in
27 Section 402(g)(3)) for the taxable year that may be excluded
28 from gross income under Section 402(g) of the Internal Revenue
29 Code, as applicable for state purposes, shall not exceed the
30 amount of elective deferrals that may be excluded from gross
31 income under Section 402(g) of the Internal Revenue Code, as
32 amended by Title VI of the Economic Growth and Tax Relief
33 Reconciliation Act of 2001 (Public Law 107-16) and Section 411
34 of the Job Creation and Worker Assistance Act of 2002 (Public
35 Law 107-147), including additional elective deferrals under
36 Section 414(v) of the Internal Revenue Code, as added by Title
37 VI of the Economic Growth and Tax Relief Reconciliation Act of
38 2001 (Public Law 107-16) and as amended by Section 411 of the
39 Job Creation and Worker Assistance Act of 2002 (Public Law
40 107-147).

1 (d) (1) For taxable years beginning on or after January 1,
2 2002, the basis of any person in the plan, account, or annuity
3 shall be increased by the amount of elective deferrals not
4 excluded as a result of the application of subdivision (c).

5 (2) Any basis described in paragraph (1) shall be recovered in
6 the manner specified in Section 17085.

7 (e) Notwithstanding the limitations provided in subdivision
8 (c), any income attributable to elective deferrals in taxable years
9 beginning on or after January 1, 2002, in conformance with Part
10 I of Subchapter D of Chapter 1 of Subtitle A of the Internal
11 Revenue Code, as applicable for federal and state purposes, shall
12 not be includable in the gross income of the individual for whose
13 benefit the plan or account was established until distributed
14 pursuant to the plan or by operation of law.

15 SEC. 35. Section 17551 of the Revenue and Taxation Code is
16 amended to read:

17 17551. (a) Subchapter E of Chapter 1 of Subtitle A of the
18 Internal Revenue Code, relating to accounting periods and
19 methods of accounting, shall apply, except as otherwise
20 provided.

21 (b) Section 444(c)(1) of the Internal Revenue Code, relating to
22 effect of election, shall not apply.

23 (c) (1) Notwithstanding the specified date contained in
24 paragraph (1) of subdivision (a) of Section 17024.5, Section 457
25 of the Internal Revenue Code, relating to deferred compensation
26 plans of state and local governments and tax-exempt
27 organizations, shall apply, except as otherwise provided, without
28 regard to taxable year to the same extent as applicable for federal
29 income tax purposes.

30 (2) The maximum deferred compensation for the taxable year
31 that may be excluded from gross income under Section 457 of
32 the Internal Revenue Code, as applicable for state purposes, shall
33 not exceed the amount of deferred compensation that may be
34 excluded from gross income under Section 457 of the Internal
35 Revenue Code, as amended by Title VI of the Economic Growth
36 and Tax Relief Reconciliation Act of 2001 (Public Law 107-16)
37 and as amended by Section 411 of the Job Creation and Worker
38 Assistance Act of 2002 (Public Law 107-147), including
39 additional elective deferrals under Section 414(v) of the Internal
40 Revenue Code, as added by Title VI of the Economic Growth

1 and Tax Relief Reconciliation Act of 2001 (Public Law 107-16)
2 and Section 411 of the Job Creation and Worker Assistance Act
3 of 2002 (Public Law 107-147).

4 (d) (1) For taxable years beginning on or after January 1,
5 2002, the basis of any person in the plan shall be increased by the
6 amount of compensation not allowed to be excluded under
7 subdivision (a).

8 (2) Any basis described in paragraph (1) shall be recovered in
9 the manner specified in Section 17085.

10 (e) Notwithstanding the limitations provided in subdivision
11 (a), any income attributable to compensation deferred in a plan in
12 taxable years beginning on or after January 1, 2002, in
13 conformance with Section 457 of the Internal Revenue Code, as
14 applicable for federal and state purposes, shall not be includable
15 in the gross income of the individual for whose benefit the plan
16 was established until distributed pursuant to the provisions of the
17 plan or by operation of law.

18 (f) Section 451(i) of the Internal Revenue Code, relating to
19 special rule for sales or dispositions to implement Federal Energy
20 Regulatory Commission or state electric restructuring policy,
21 shall not apply.

22 SEC. 36. Section 17681.6 is added to the Revenue and
23 Taxation Code, to read:

24 17681.6. Section 613A(c)(6)(H) of the Internal Revenue
25 Code, relating to temporary suspension of taxable income limit
26 with respect to marginal production, shall not apply.

27 SEC. 37. Section 17731 of the Revenue and Taxation Code is
28 amended to read:

29 17731. (a) Subchapter J of Chapter 1 of Subtitle A of the
30 Internal Revenue Code, relating to estates, trusts, beneficiaries,
31 and decedents, shall apply, except as otherwise provided.

32 (b) Section 692(d)(2) of the Internal Revenue Code, relating to
33 the ten thousand-dollar (\$10,000) minimum benefit, does not
34 apply.

35 SEC. 37.5. *Section 17733 of the Revenue and Taxation Code*
36 *is amended to read:*

37 17733. (a) An estate shall be allowed a credit of ten dollars
38 (\$10) against the tax imposed under Section 17041, less any
39 amounts imposed under paragraph (1) of subdivision (d) or
40 paragraph (1) of subdivision (e), or both, of Section 17560.

(b) (1) Except as provided in paragraph (2), a trust shall be allowed a credit of one dollar (\$1) against the tax imposed under Section 17041, less any amounts imposed under paragraph (1) of subdivision (d) or paragraph (1) of subdivision (e), or both, of Section 17560.

(2) (A) A disability trust, as defined in ~~Internal Revenue Code~~ Section 642(b)(2)(C) *of the Internal Revenue Code, as amended by the Victims of Terrorism Tax Relief Act of 2001 (Public Law 107-134)*, shall be allowed a credit in an amount equal to the personal exemption credit authorized for a single individual pursuant to subdivision (a) of Section 17054.

(B) The credit authorized by subparagraph (A) shall be subject to the credit reduction provisions of Section 17054.1. For purposes of making the adjustments required by Section 17054.1, the adjusted gross income of the disability trust shall be computed in accordance with ~~Internal Revenue Code~~ Section 167(e) *67(e) of the Internal Revenue Code, relating to determination of adjusted gross income in case of estates and trusts.*

(C) This paragraph applies to taxable years beginning on or after January 1, 2004.

(c) The credits allowed by this section shall be in lieu of the credits allowed under Section 17054 (relating to credit for personal exemption).

SEC. 37.6. Section 17734.6 is added to the Revenue and Taxation Code, to read:

17734.6. Section 646 of the Internal Revenue Code, relating to tax treatment of electing Alaska Native Settlement Trusts, shall not apply.

SEC. 38. Section 17760 is added to the Revenue and Taxation Code, to read:

17760. Section 684 of the Internal Revenue Code, relating to recognition of gain on certain transfers to certain foreign trusts and estates, shall not apply.

SEC. 39. Section 18035.6 is added to the Revenue and Taxation Code, to read:

18035.6. Section 1014 of the Internal Revenue Code, relating to basis of property acquired from a decedent, is modified to provide that Section 1014(f) of the Internal Revenue Code, relating to termination date, shall not apply.

1 SEC. 40. Section 18036.6 is added to the Revenue and
2 Taxation Code, to read:

3 18036.6. Section 1022 of the Internal Revenue Code, relating
4 to treatment of property acquired from a decedent dying after
5 December 31, 2009, shall not apply.

6 *SEC. 40.5. Section 18181 is added to the Revenue and*
7 *Taxation Code, to read:*

8 *18181. Part VI of Subchapter P of Chapter 1 of Subtitle A of*
9 *the Internal Revenue Code, relating to treatment of certain*
10 *passive foreign investment companies, shall not apply.*

11 SEC. 41. Section 18571 of the Revenue and Taxation Code
12 is amended to read:

13 18571. (a) The provisions of Section 7508 of the Internal
14 Revenue Code, relating to time for performing certain acts
15 postponed by reason of service in a combat zone or contingency
16 operation, shall apply except as otherwise provided.

17 (b) Section 7508(e)(1) of the Internal Revenue Code, relating
18 to tax in jeopardy, etc., is modified to refer to jeopardy
19 assessments and liens authorized under this part, in lieu of the
20 references to Section 6851 and Chapter 70 or 71 of the Internal
21 Revenue Code.

22 (c) Notwithstanding Section 17034, this section shall be
23 operative without regard to taxable years and shall be operative
24 with respect to any actions specified in Section 18570 that are
25 required or permitted to be taken on or after August 2, 1990.

26 SEC. 42. Section 18572 of the Revenue and Taxation Code
27 is amended to read:

28 18572. Section 7508A of the Internal Revenue Code, relating
29 to postponement of certain tax-related deadlines, shall apply,
30 except as otherwise provided.

31 *SEC. 42.5. Section 18628 of the Revenue and Taxation Code*
32 *is amended to read:*

33 18628. (a) Section 6111 of the Internal Revenue Code,
34 relating to ~~registration of tax shelters~~ *disclosure of reportable*
35 *transactions*, applies, except as otherwise provided.

36 (b) (1) Except as provided in subdivision ~~(g)~~ *(e)*, a ~~tax shelter~~
37 ~~organizer~~ *material advisor* is required to send a duplicate of the
38 federal ~~registration information return~~, if applicable, or the same
39 information required ~~for to be provided on the federal tax shelters~~
40 *reportable transactions return* for California ~~tax shelters~~

1 *reportable transactions* to the Franchise Tax Board not later than
2 ~~the day on which the first offering for sale of interests in that tax~~
3 ~~shelter occurs~~ *date specified by the Franchise Tax Board or the*
4 *Secretary of the Treasury.*

5 (2) (A) The information provided to the Franchise Tax Board
6 pursuant to paragraph (1) shall also include any other information
7 required by a Franchise Tax Board Notice.

8 (B) Chapter 3.5 (commencing with Section 11340) of Part 1 of
9 Division 3 of Title 2 of the Government Code does not apply to
10 any additional information requested under this section.

11 ~~(c) Any person required to register under Section 6111 of the~~
12 ~~Internal Revenue Code who receives a tax registration number~~
13 ~~from the Secretary of the Treasury shall, within 30 days after~~
14 ~~request by the Franchise Tax Board, file a statement of that~~
15 ~~registration number~~ *Section 6111 of the Internal Revenue Code is*
16 *modified by substituting the phrase “Secretary of the Franchise*
17 *Tax Board” for the word “Secretary” in each place it appears.*

18 ~~(d) Section 6111(b) of the Internal Revenue Code, relating to~~
19 ~~inclusion of tax shelter identification numbers on returns, applies.~~

20 ~~(e) Section 6111(e)(2)(A) of the Internal Revenue Code is~~
21 ~~amended by substituting the phrase “under subtitle A of the~~
22 ~~Internal Revenue Code or under this part, Part 10 (commencing~~
23 ~~with Section 17001), or Part 11 (commencing with Section~~
24 ~~23001) of the Revenue and Taxation Code” for “under subtitle~~
25 ~~A”.~~

26 ~~(f) (1) Section 6111(d) of the Internal Revenue Code is~~
27 ~~modified to further provide that, for purposes of this section and~~
28 ~~Section 18648, the term “tax shelter” includes any listed~~
29 ~~transaction (as defined under subdivision (a) of Section 18407).~~

30 ~~(2) Section 6111(d)(1)(A) of the Internal Revenue Code is~~
31 ~~amended by substituting the phrase “avoidance or evasion of~~
32 ~~federal income tax or California income or franchise tax” for~~
33 ~~“avoidance or evasion of Federal income tax.”~~

34 ~~(g)~~

35 ~~(d) The—registration~~ *reportable transactions return*
36 *requirements of this section shall apply to any tax shelter (within*
37 *the meaning of Section 6111 material advisor with respect to any*
38 *reportable transaction, as defined in Section 6707A(c) of the*
39 *Internal Revenue Code, as modified by this section) that*

1 ~~additionally~~ *with respect to a material advisor that satisfies any*
2 *of the following conditions:*

- 3 (1) ~~Organized~~ *Is organized* in this state.
4 (2) ~~Doing~~ *Is doing* business in this state.
5 (3) ~~Deriving~~ *Derives* income from sources in this state.
6 (4) ~~At least one of its investors is a California taxpayer.~~

7 *Provides any material aid, assistance, or advice with respect to*
8 *organizing, managing, promoting, selling, implementing,*
9 *insuring, or carrying out any reportable transaction with respect*
10 *to a taxpayer that meets any of the following requirements:*

- 11 ~~(h)~~
12 (A) *Is organized in this state.*
13 (B) *Does business in this state.*
14 (C) *Derives income from sources in this state.*
15 (e) In addition to the requirements set forth in subdivision (a),
16 for any transactions entered into on or after February 28, 2000,
17 that become listed transactions (as defined under Section 6011(a)
18 6707A(c)(2) of the Internal Revenue Code) at any time, *a return*
19 *for those transactions shall be required to be registered filed with*
20 *the Franchise Tax Board by the later of:*

- 21 (1) Sixty days after entering into the transaction.
22 (2) Sixty days after the transaction becomes a listed
23 transaction.
24 (3) ~~April 30, 2004~~ *Sixty days after the effective date of the act*
25 *amending this section.*

- 26 ~~(i)~~
27 (f) In addition to the requirements set forth in subdivisions (a)
28 and ~~(h)~~ (e), for any transactions entered into on or after
29 September 2, 2003, that are specifically identified by the
30 Franchise Tax Board for California income or franchise tax
31 purposes (under the authority of paragraph (4) of subdivision (a)
32 of Section 18407) as a “listed transaction” at any time, *a return*
33 *for those transactions shall be required to be registered filed with*
34 *the Franchise Tax Board by the later of:*

- 35 (1) Sixty days after entering into the transaction.
36 (2) Sixty days after the transaction becomes a listed
37 transaction.
38 (3) ~~April 30, 2004~~ *Sixty days after the effective date of the act*
39 *amending this section.*

1 SEC. 43. Section 18633 of the Revenue and Taxation Code is
2 amended to read:

3 18633. (a) (1) Every partnership, on or before the 15th day
4 of the fourth month following the close of its taxable year, shall
5 make a return for that taxable year, stating specifically the items
6 of gross income and the deductions allowed by Part 10
7 (commencing with Section 17001). Except as otherwise provided
8 in Section 18621.5, the return shall include the names, addresses,
9 and taxpayer identification numbers of the persons, whether
10 residents or nonresidents, who would be entitled to share in the
11 net income if distributed and the amount of the distributive share
12 of each person. The return shall contain or be verified by a
13 written declaration that it is made under penalty of perjury,
14 signed by one of the partners.

15 (2) In addition to returns required by paragraph (1), every
16 limited partnership subject to the tax imposed by subdivision (b)
17 of Section 17935, on or before the 15th day of the fourth month
18 following the close of its taxable year, shall make a return for
19 that taxable year, containing the information identified in
20 paragraph (1). In the case of a limited partnership not doing
21 business in this state, the Franchise Tax Board shall prescribe the
22 manner and extent to which the information identified in
23 paragraph (1) shall be included with the return required by this
24 paragraph.

25 (b) Each partnership required to file a return under subdivision
26 (a) for any taxable year shall (on or before the day on which the
27 return for that taxable year was required to be filed) furnish to
28 each person who is a partner or who holds an interest in that
29 partnership as a nominee for another person at any time during
30 that taxable year a copy of the information required to be shown
31 on that return as may be required by regulations.

32 (c) Any person who holds an interest in a partnership as a
33 nominee for another person shall do both of the following:

34 (1) Furnish to the partnership, in the manner prescribed by the
35 Franchise Tax Board, the name, address, and taxpayer
36 identification number of that other person, and any other
37 information for that taxable year as the Franchise Tax Board may
38 by form and regulation prescribe.

(2) Furnish to that other person, in the manner prescribed by the Franchise Tax Board, the information provided by that partnership under subdivision (b).

(d) The provisions of Section 6031(d) of the Internal Revenue Code, relating to the separate statement of items of unrelated business taxable income, shall apply.

(e) The provisions of Section 6031(f) of the Internal Revenue Code, relating to electing investment partnerships, shall apply, except as otherwise provided.

SEC. 43.5. Section 18648 of the Revenue and Taxation Code is amended to read:

18648. (a) Section 6112 of the Internal Revenue Code, relating to ~~organizers and sellers of potentially abusive tax shelters that~~ material advisors of reportable transactions that must keep lists of investors advisees, applies except as otherwise provided.

(b) Section 6112 of the Internal Revenue Code is modified by substituting the phrase “Secretary or the Franchise Tax Board” for the word “Secretary” each place it appears.

(c) The requirement to maintain lists under this section shall apply to any ~~organizer, seller or material advisor of a potentially abusive tax shelter (within the meaning of Section 6112, as defined in Section 6111 of the Internal Revenue Code, with respect to any reportable transaction, as defined in Section 6707A(c) of the Internal Revenue Code, as modified by this section)~~ and regardless of whether a return is required to be filed under Section 18628 with respect to that reportable transaction and with respect to a material advisor that ~~additionally~~ satisfies any of the following conditions:

- (1) ~~Organized~~ *Is organized* in this state.
- (2) ~~Doing~~ *Is doing* business in this state.
- (3) ~~Deriving~~ *Derives* income from sources in this state.
- (4) ~~At least one of its investors is a California taxpayer.~~ *Provides any material aid, assistance, or advice with respect to organizing, managing, promoting, selling, implementing, insuring, or carrying out any reportable transaction with respect to a taxpayer that meets any of the following conditions:*
 - (A) *Is organized in this state.*
 - (B) *Does business in this state.*
 - (C) *Derives income from sources in this state.*

(d) (1) ~~Notwithstanding~~ *In addition to* any regulation issued under Section 6112 of the Internal Revenue Code, the list required to be maintained by this section for listed transactions, as defined in ~~subdivision (a) of Section 18407~~ *Section 6707A(c)(2) of the Internal Revenue Code*, shall be maintained in the form and manner prescribed by the Franchise Tax Board.

(2) Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code does not apply to any requirement prescribed by the Franchise Tax Board under this section.

(3) For transactions entered into on or after February 28, 2000, that become listed transactions (as defined under ~~Section 6011(a) 6707A(c)(2)~~ of the Internal Revenue Code) at any time, the lists shall be provided to the Franchise Tax Board by the later of:

(A) Sixty days after entering into the transaction.

(B) Sixty days after the transaction becomes a listed transaction.

~~(C) April 30, 2004.~~

(4) For transactions entered into on or after September 2, 2003, that are specifically identified by the Franchise Tax Board for California income or franchise tax purposes (under the authority of paragraph (4) of subdivision (a) of Section 18407) as a “listed transaction” at any time, the list shall be provided to the Franchise Tax Board by the later of:

(A) Sixty days after entering into the transaction.

(B) Sixty days after the transaction becomes a listed transaction.

~~(C) April 30, 2004.~~

~~(e) The terms “organizer,” “seller,” and “material advisor” mean a person that meets any of the requirements of this section or of Section 6112 of the Internal Revenue Code or regulations issued thereunder.~~

SEC. 44. Section 19008 of the Revenue and Taxation Code is amended to read:

19008. (a) The Franchise Tax Board may, in cases of financial hardship, as determined by the Franchise Tax Board, allow an individual or fiduciary to enter into installment payment agreements with the Franchise Tax Board to make payments on taxes due, plus applicable interest and penalties over the life of the installment period. Failure by an individual or fiduciary to

1 comply fully with the terms of the installment payment
2 agreement shall render the agreement null and void, unless the
3 Franchise Tax Board determines that the failure was due to a
4 reasonable cause, and the total amount of tax, interest, and all
5 penalties shall be immediately due and payable.

6 (b) In the case of a liability for tax of an individual under Part
7 10 (commencing with Section 17001) or this part, the Franchise
8 Tax Board shall enter into an agreement to accept the full
9 payment of the tax in installments if, as of the date the individual
10 offers to enter into the agreement, all of the following apply:

11 (1) The aggregate amount of the liability (determined without
12 regard to interest, penalties, additions to the tax and additional
13 amounts) does not exceed ten thousand dollars (\$10,000).

14 (2) The taxpayer (and, if the liability relates to a joint return,
15 the taxpayer's spouse) has not during any of the preceding five
16 taxable years done any of the following:

17 (A) Failed to file any return of tax imposed under Part 10
18 (commencing with Section 17001) or this part.

19 (B) Failed to pay any tax required to be shown on the return.

20 (C) Entered into an installment agreement under this section
21 for payment of any tax imposed by Part 10 (commencing with
22 Section 17001) or this part.

23 (3) The Franchise Tax Board determines that the taxpayer is
24 financially unable to pay the liability in full when due (and the
25 taxpayer submits any information as the Franchise Tax Board
26 may require to make this determination).

27 (4) The agreement requires full payment of the liability within
28 three years.

29 (5) The taxpayer agrees to comply with the provisions of this
30 part and Part 10 (commencing with Section 17001) for the period
31 the agreement is in effect.

32 (c) Except in any case where the Franchise Tax Board finds
33 collection of the tax to which an installment payment agreement
34 relates to be in jeopardy, or there is a mutual consent to
35 terminate, alter, or modify the agreement, the agreement shall not
36 be considered null and void, or otherwise terminated, unless both
37 of the following occur:

38 (1) A notice of termination is provided to the individual or
39 fiduciary not later than 30 days before the date of termination.

1 (2) The notice includes an explanation of why the Franchise
2 Tax Board intends to terminate the agreement.

3 (d) No levy may be issued on the property or rights to property
4 of any person with respect to any unpaid tax:

5 (1) During the period that an offer by the taxpayer for an
6 installment agreement under this section for payment of the
7 unpaid tax is pending with the Franchise Tax Board.

8 (2) If the offer is rejected by the Franchise Tax Board, during
9 the 30 days thereafter (and, if a request for review of the rejection
10 is filed within the 30 days, during the period that the review is
11 pending).

12 (3) During the period that the installment agreement for
13 payment of the unpaid tax is in effect.

14 (4) If the agreement is terminated by the Franchise Tax Board,
15 during the 30 days thereafter (and, if a request for review of the
16 termination is filed within the 30 days, during the period that the
17 review is pending).

18 (5) This subdivision shall not apply with respect to any of the
19 following:

20 (A) Any unpaid tax if either of the following occurs:

21 (i) The taxpayer files a written notice with the Franchise Tax
22 Board that waives the restriction imposed by this subdivision on
23 levy with respect to the tax.

24 (ii) The Franchise Tax Board finds that the collection of that
25 tax is in jeopardy.

26 (B) Any levy that was first issued before the date that the
27 applicable proceeding under this subdivision commenced.

28 (C) At the discretion of the Franchise Tax Board, any unpaid
29 tax for which the taxpayer makes an offer of an installment
30 agreement subsequent to a rejection of an offer of an installment
31 agreement with respect to that unpaid tax (or to any review
32 thereof).

33 (D) The period of limitation under Section 19371 shall be
34 suspended for the period during which the Franchise Tax Board
35 is prohibited under this subdivision from making a levy.

36 (e) The Taxpayers' Rights Advocate shall establish procedures
37 for an independent departmental administrative review for the
38 rejection of the offer of an installment payment and for
39 installment payment agreements that are rendered null and void,
40 or otherwise terminated under this section, for individuals or

1 fiduciaries who request that review. This administrative review
2 shall not be subject to Chapter 4.5 (commencing with Section
3 11400) of Part 1 of Division 3 of the Government Code. Unless
4 review is requested by the taxpayer within 30 days of the date of
5 rejection of the offer of an installment agreement or termination
6 of the installment agreement, this administrative review shall not
7 stay collection of the tax to which the installment payment
8 agreement relates.

9 (f) In the case of an agreement for partial payment of a tax
10 liability entered into by the Franchise Tax Board pursuant to
11 subdivision (a), the Franchise Tax Board shall review the
12 agreement at least once every two years.

13 (g) The amendments made by the act adding this subdivision
14 are operative for any proposed installment agreement submitted
15 after the effective date of that act.

16 SEC. 45. Section 19041.5 of the Revenue and Taxation Code
17 is amended to read:

18 19041.5. (a) Notwithstanding any other provision of this
19 part, Part 10 (commencing with Section 17001), or Part 11
20 (commencing with Section 23001), the provisions of Section
21 6603 of the Internal Revenue Code, relating to deposits made to
22 suspend the running of interest on potential underpayments, shall
23 ~~apply~~ *apply*, except as otherwise provided. A deposit shall not be
24 considered a payment of tax for purposes of filing a claim for
25 refund pursuant to Section 19306, converting an administrative
26 action to an action on a claim pursuant to Section 19335, or filing
27 an action pursuant to Section ~~19384~~ 19384, until either of the
28 following occurs:

29 (1) The taxpayer provides a written statement to the Franchise
30 Tax Board specifying that the deposit shall be a payment of tax
31 for purposes of Section 19306, 19335, or 19384.

32 (2) The deposit is used to pay a final tax liability.

33 (b) Section 6603(d) of the Internal Revenue Code is modified
34 to substitute the phrase “notice of proposed deficiency
35 assessment under Article 3 of Chapter 4 of this part” for “30-day
36 letter” in each place that the phrase “30-day letter” appears.

37 (c) In the case of ~~an~~ *any* amount held by the Franchise Tax
38 Board as a deposit in the nature of a cash bond pursuant to the
39 provisions of this section prior to the amendments made by the
40 act adding this subdivision, the date that the taxpayer identifies

1 that amount as a deposit made pursuant to this ~~section~~ *section*, as
2 amended by the act adding this ~~subdivision~~ *subdivision*, shall be
3 treated as the date that the amount is deposited for purposes of
4 this ~~section~~ *section*, as amended by the act adding this
5 subdivision.

6 SEC. 46. Section 19116 of the Revenue and Taxation Code is
7 amended to read:

8 19116. (a) In the case of an individual who files a return of
9 tax imposed under Part 10 (commencing with Section 17001) for
10 a taxable year on or before the due date for the return, including
11 extensions, if the Franchise Tax Board does not provide a notice
12 to the taxpayer specifically stating the taxpayer's liability and the
13 basis of the liability before the close of the notification period,
14 the Franchise Tax Board shall suspend the imposition of any
15 interest, penalty, addition to tax, or additional amount with
16 respect to any failure relating to the return which is computed by
17 reference to the period of time the failure continues to exist and
18 which is properly allocable to the suspension period.

19 (b) For purposes of this section:

20 (1) Except as provided in subdivision (e), "notification period"
21 means the 18-month period beginning on the later of either of the
22 following:

23 (A) The date on which the return is filed.

24 (B) The due date of the return without regard to extensions.

25 (2) "Suspension period" means the period beginning on the
26 day after the close of the notification period and ending on the
27 date which is 15 days after the date on which notice described in
28 subdivision (a) is provided by the Franchise Tax Board.

29 (c) This section shall be applied separately with respect to
30 each item or adjustment.

31 (d) This section shall not apply to any of the following:

32 (1) Any penalty imposed by Section 19131.

33 (2) Any penalty imposed by Section 19132.

34 (3) Any interest, penalty, addition to tax, or additional amount
35 involving fraud.

36 (4) Any interest, penalty, addition to tax, or additional amount
37 with respect to any tax liability shown on the return.

38 (5) Any criminal penalty.

1 (6) Any interest, penalty, addition to tax, or additional amount
2 ~~with respect to any reportable transaction and any listed~~
3 ~~transaction.~~ *with respect to any gross misstatement.*

4 (7) *Any interest, penalty, addition to tax, or additional amount*
5 *relating to any reportable transaction with respect to which the*
6 *requirements of Section 6664(d)(2)(A) of the Internal Revenue*
7 *Code are not met, and any listed transaction, as defined in*
8 *Section 6707A(c) of the Internal Revenue Code.*

9 (e) For taxpayers required by subdivision (a) of Section 18622
10 to report a change or correction by the Commissioner of Internal
11 Revenue or other officer of the United States or other competent
12 authority the following rules shall apply:

13 (1) The notification period under subdivision (a) shall be
14 either of the following:

15 (A) One year from the date the notice required by Section
16 18622 is filed with the Franchise Tax Board by the taxpayer or
17 the Internal Revenue Service, if the taxpayer or the Internal
18 Revenue Service reports that change or correction within six
19 months after the final federal determination.

20 (B) Two years from the date when the notice required by
21 Section 18622 is filed with the Franchise Tax Board by the
22 taxpayer or the Internal Revenue Service, if after the six-month
23 period required in Section 18622, a taxpayer or the Internal
24 Revenue Service reports a change or correction.

25 (2) The suspension period under subdivision (a) shall mean the
26 period beginning on the day after the close of the notification
27 period under paragraph (1) and ending on the date which is 15
28 days after the date on which notice described in subdivision (a) is
29 provided by the Franchise Tax Board.

30 (f) For notices sent after January 1, 2004, this section does not
31 apply to taxpayers with taxable income greater than two hundred
32 thousand dollars (\$200,000) that have been contacted by the
33 Franchise Tax Board regarding the use of a potentially abusive
34 tax shelter (within the meaning of Section 19777).

35 (g) This section shall apply to taxable years ending after
36 October 10, 1999.

37 (h) *The amendments made to this section by the act adding*
38 *this subdivision shall apply to notices sent after January 1, 2005.*

39 SEC. 47. *Section 19136.12 is added to the Revenue and*
40 *Taxation Code, to read:*

1 19136.12. (a) No addition to tax shall be made pursuant to
2 Section 19136 for any period before the date prescribed under
3 Section 18566 for the filing of the return for the 2005 taxable
4 year, with respect to any underpayment of an installment for the
5 2005 taxable year, to the extent that the underpayment was
6 created or increased by any provision of the act adding this
7 section.

8 (b) No addition to tax shall be made pursuant to Section
9 18601 for the filing of the return for the 2005 taxable year, with
10 respect to any underpayment of an installment for the 2005
11 taxable year, to the extent that the underpayment was created or
12 increased by any provision of the act adding this section.

13 (c) The Franchise Tax Board shall implement this section in a
14 reasonable manner.

15 ~~SEC. 47. Section 19136.7 is added to the Revenue and~~
16 ~~Taxation Code, to read:~~

17 ~~19136.7. (a) No addition to tax shall be made pursuant to~~
18 ~~Section 19136 for any period before the date prescribed under~~
19 ~~Section 18566 for the filing of the return for the 2005 taxable~~
20 ~~year, with respect to any underpayment of an installment for the~~
21 ~~2005 taxable year, to the extent that the underpayment was~~
22 ~~created or increased by any provision of the act adding this~~
23 ~~section.~~

24 ~~(b) No addition to tax shall be made pursuant to Section 18601~~
25 ~~for the filing of the return for the 2005 taxable year, with respect~~
26 ~~to any underpayment of an installment for the 2005 taxable year,~~
27 ~~to the extent that the underpayment was created or increased by~~
28 ~~any provision of the act adding this section.~~

29 ~~(c) The Franchise Tax Board shall implement this section in a~~
30 ~~reasonable manner.~~

31 ~~SEC. 47.1. Section 19164 of the Revenue and Taxation Code~~
32 ~~is amended to read:~~

33 19164. (a) (1) (A) An accuracy-related penalty shall be
34 imposed under this part and shall be determined in accordance
35 with Section 6662 of the Internal Revenue Code, relating to
36 imposition of accuracy-related penalty *on underpayments*, except
37 as otherwise provided.

38 (B) (i) Except for understatements relating to ~~tax shelter items~~
39 ~~reportable transactions to which paragraph (5) Section 19164.5~~
40 ~~applies~~, in the case of any proposed deficiency assessment issued

1 after the last date of the amnesty period specified in Chapter 9.1
2 (commencing with Section 19730) for any taxable year
3 beginning prior to January 1, 2003, the penalty specified in
4 Section 6662(a) of the Internal Revenue Code shall be computed
5 by substituting “40 percent” for “20 percent.”

6 (ii) Clause (i) shall not apply to any taxable year of a taxpayer
7 beginning prior to January 1, 2003, if, as of the start date of the
8 amnesty program period specified in Section 19731, the taxpayer
9 is then under audit by the Franchise Tax Board, or the taxpayer
10 has filed a protest under Section 19041, or the taxpayer has filed
11 an appeal under Section 19045, or the taxpayer is engaged in
12 settlement negotiations under Section 19442, or the taxpayer has
13 a pending judicial proceeding in any court of this state or in any
14 federal court relating to the tax liability of the taxpayer for that
15 taxable year.

16 (2) With respect to corporations, this subdivision shall apply to
17 all of the following:

18 (A) All taxable years beginning on or after January 1, 1990.

19 (B) Any other taxable year for which an assessment is made
20 after July 16, 1991.

21 (C) For purposes of this section, references in Section 6662(e)
22 of the Internal Revenue Code and the regulations thereunder,
23 relating to treatment of an affiliated group that files a
24 consolidated federal return, are modified to apply to those
25 entities required to be included in a combined report under
26 Section 25101 or 25110. For these purposes, entities included in
27 a combined report pursuant to paragraph (4) or (6) of subdivision
28 (a) of Section 25110 shall be considered only to the extent
29 required to be included in the combined report.

30 (3) Section 6662(d)(1)(B) of the Internal Revenue Code is
31 modified to provide that in the case of a corporation, other than
32 an “S” corporation, ~~that has been contacted by the Franchise Tax~~
33 ~~Board regarding the use of a potentially abusive tax shelter~~
34 ~~(within the meaning of Section 19777),~~ there is a substantial
35 understatement of tax for any taxable year if the amount of the
36 understatement for the taxable year exceeds the lesser of:

37 (A) Ten percent of the tax required to be shown on the return
38 for the taxable year (or, if greater, two thousand five hundred
39 dollars (\$2,500)).

40 (B) Five million dollars (\$5,000,000).

(4) Section 6662(d)(2)(A) of the Internal Revenue Code is modified to additionally provide that the excess determined under Section 6662(d)(2)(A) of the Internal Revenue Code shall be determined without regard to items to which Section ~~19773~~ 19164.5 applies and without regard to items with respect to which a penalty is imposed by Section 19774.

~~(5) For taxpayers that have been contacted by the Franchise Tax Board regarding the use of a potentially abusive tax shelter (within the meaning of Section 19777), Section 6662(d)(2)(B)(i) of the Internal Revenue Code is modified to substitute the phrase “the tax treatment of any item by the taxpayer if the taxpayer had reasonable belief that the tax treatment was more likely than not the proper treatment” for the phrase “the tax treatment of any item by the taxpayer if there is or was substantial authority for such treatment” contained therein.~~

(b) For purposes of Section 6662(d) of the Internal Revenue Code, Section 6664 of the Internal Revenue Code ~~(as modified by subdivision (d))~~, Section 6694(a)(1) of the Internal Revenue Code, and this part, the Franchise Tax Board may prescribe a list of positions for which the Franchise Tax Board believes there is not substantial authority or there is no reasonable belief that the tax treatment is more likely than not the proper tax treatment. That list (and any revisions thereof) shall be published through the use of Franchise Tax Board Notices or other published positions. In addition, the “listed transactions” identified and published pursuant to the preceding sentence shall be published on the Web site of the Franchise Tax Board. ~~This subdivision applies only to list of positions relating to abusive tax shelters, within the meaning of Section 19777.~~

(c) A fraud penalty shall be imposed under this part and shall be determined in accordance with Section 6663 of the Internal Revenue Code, relating to imposition of fraud penalty, except as otherwise provided.

(d) Section 6664 of the Internal Revenue Code, relating to definitions and special rules, shall apply, except as otherwise provided.

~~(1) For taxpayers that have been contacted by the Franchise Tax Board regarding the use of a potentially abusive tax shelter (within the meaning of Section 19777), Section 6664 of the Internal Revenue Code is modified to additionally provide that~~

1 no penalty shall be imposed under Section 19773 with respect to
2 any portion of a reportable transaction understatement if it is
3 shown that there was a reasonable cause for that portion and that
4 the taxpayer acted in good faith with respect to that portion.

5 (2) Paragraph (1) does not apply to any reportable transaction
6 understatement unless all of the following requirements are met:

7 (A) (i) The relevant facts affecting the tax treatment of the
8 item are adequately disclosed in accordance with the regulations
9 prescribed under Section 6011 of the Internal Revenue Code, as
10 modified by Section 18407.

11 (ii) A taxpayer failing to adequately disclose in accordance
12 with Section 6011 of the Internal Revenue Code, as modified by
13 Section 18407, shall be treated as meeting the requirements of
14 this subparagraph, if the penalty for that failure was rescinded
15 under subdivision (c) of Section 19772.

16 (iii) For taxable years beginning on or before January 1, 2003,
17 “adequately disclosed” includes the disclosure of the tax shelter
18 identification number on the taxpayer’s return, as required by
19 subdivision (e) of Section 18628.

20 (B) There is or was substantial authority for that treatment.

21 (C) The taxpayer reasonably believed that treatment was more
22 likely than not the proper treatment.

23 (3) For purposes of subparagraph (C) of paragraph (2) all of
24 the following shall apply:

25 (A) A taxpayer shall be treated as having a reasonable belief
26 with respect to the tax treatment of an item only if that belief
27 meets both of the following requirements:

28 (i) Is based on the facts and law that exist at the time the return
29 of tax that includes that tax treatment is filed.

30 (ii) Relates solely to the taxpayer’s chances of success on the
31 merits of that treatment and does not take into account the
32 possibility that the return will not be audited, that the treatment
33 will not be raised on audit, or that the treatment will be resolved
34 through settlement if it is raised.

35 (B) (i) An opinion of a tax advisor may not be relied upon to
36 establish the reasonable belief of a taxpayer if either of the
37 following conditions are met:

38 (I) The tax advisor is described in clause (ii).

39 (II) The opinion is described in clause (iii).

1 (ii) ~~A tax advisor is described in this clause if the tax advisor~~
2 ~~meets any of the following conditions:~~

3 (I) ~~Is a material advisor (within the meaning of subdivision (d)~~
4 ~~of Section 18648) who participates in the organization,~~
5 ~~management, promotion, or sale of the transaction or who is~~
6 ~~related (within the meaning of Section 267(b) or 707(b)(1) of the~~
7 ~~Internal Revenue Code) to any person who so participates.~~

8 (II) ~~Is compensated directly or indirectly by a material advisor~~
9 ~~with respect to the transaction.~~

10 (III) ~~Has a fee arrangement with respect to the transaction that~~
11 ~~is contingent on all or part of the intended tax benefits from the~~
12 ~~transaction being sustained.~~

13 (IV) ~~As determined under regulations prescribed by either the~~
14 ~~Secretary of the Treasury for federal income tax purposes or the~~
15 ~~Franchise Tax Board, has a continuing financial interest with~~
16 ~~respect to the transaction.~~

17 (iii) ~~For purposes of clause (i), an opinion is disqualified if the~~
18 ~~opinion meets any of the following conditions:~~

19 (I) ~~Is based on unreasonable, factual, or legal assumptions~~
20 ~~(including assumptions as to future events).~~

21 (II) ~~Unreasonably relies on representations, statements,~~
22 ~~findings, or agreements of the taxpayer or any other person.~~

23 (III) ~~Does not identify and consider all relevant facts.~~

24 (IV) ~~Fails to meet any other requirement as either the~~
25 ~~Secretary of the Treasury for federal income tax purposes or the~~
26 ~~Franchise Tax Board may by forms and instructions prescribe.~~

27 (e) ~~Section 6665 of the Internal Revenue Code, relating to~~
28 ~~applicable rules, shall apply, except as otherwise provided.~~

29 (f) ~~For taxpayers that have been contacted by the Franchise~~
30 ~~Tax Board regarding the use of a potentially abusive tax shelter~~
31 ~~(within the meaning of Section 19777), Section 461(i)(3)(C) of~~
32 ~~the Internal Revenue Code is modified by substituting a reference~~
33 ~~to “Section 1274(b)(3)(B) of the Internal Revenue Code, as~~
34 ~~modified by subdivision (g) of Section 19164” instead of the~~
35 ~~reference to “Section 6662(d)(2)(C)(iii)” contained therein.~~

36 (g) ~~For taxpayers that have been contacted by the Franchise~~
37 ~~Tax Board regarding the use of a potentially abusive tax shelter~~
38 ~~(within the meaning of Section 19777), Section 1274(b)(3)(B)(i)~~
39 ~~of the Internal Revenue Code is modified to provide that for~~
40 ~~purposes of Section 1274(b)(3)(B) of the Internal Revenue Code,~~

~~the term “tax shelter” means (1) a partnership or other entity, (2) any investment plan or arrangement, or (3) any other plan or arrangement, if a significant purpose of the partnership, entity, plan, or arrangement is the avoidance or evasion of federal income tax or the tax imposed under Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001).~~

SEC. 47.2. Section 19164.5 is added to the Revenue and Taxation Code, to read:

19164.5. (a) A reportable transaction accuracy-related penalty shall be imposed under this part and shall be determined in accordance with Section 6662A of the Internal Revenue Code, relating to the imposition of an accuracy-related penalty on understatements with respect to reportable transactions, except as otherwise provided.

(b) (1) The reportable transaction understatement, as determined under Section 6662A(b) of the Internal Revenue Code, is modified to not include amounts to which the penalty of Section 19774 is imposed.

(2) Section 6662A(b)(1)(A)(ii) of the Internal Revenue Code is modified to substitute the phrase “Sections 17041, 23151, 23181, or 23501” for “section 11 (section 11 in the case of a taxpayer which is a corporation).”

(3) Section 6662A(b)(1)(B) of the Internal Revenue Code is modified to substitute the phrase “Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001)” for “subtitle A.”

(4) Section 6662A(b)(2)(B) of the Internal Revenue Code is modified to substitute the phrase “income or franchise tax” for “Federal income tax.”

(5) Section 6662A(e)(1) of the Internal Revenue Code is modified to additionally provide that the amount of the understatement is increased by noneconomic transaction understatements, as defined in Section 19774.

(c) Section 6662A(e)(2) of the Internal Revenue Code is modified to additionally provide that Section 6662A of the Internal Revenue Code does not apply to amounts to which a penalty is imposed under Section 19774.

(d) The provisions of subdivision (f) of Section 19772, relating to the rescission of the penalty by the Chief Counsel, shall apply to any penalty imposed by this section.

SEC. 47.3. *Section 19166 of the Revenue and Taxation Code is amended to read:*

19166. (a) A penalty shall be imposed for understatement of any taxpayer's liability by a tax return preparer. The penalty preparer and shall be determined in accordance with Section 6694 of the Internal Revenue Code, except as otherwise provided.

~~(a)~~

(b) (1) For taxpayers that have been contacted by the Franchise Tax Board regarding the use of a potentially abusive tax shelter (within the meaning of Section 19777), a reportable transaction, as defined in Section 6707A(c)(1) of the Internal Revenue Code, with respect to which the requirements of Section 6664(d)(2)(A) of the Internal Revenue Code are not met, any listed transaction, as defined in Section 6707A(c)(2) of the Internal Revenue Code, or a gross misstatement within the meaning of Section 6404(g)(2)(D) of the Internal Revenue Code, Section 6694(a) of the Internal Revenue Code is modified to substitute "one thousand dollars (\$1,000)" for "two hundred fifty dollars (\$250)."

(2) Section 6694(a)(1) of the Internal Revenue Code is modified to substitute the phrase "reasonable belief that the tax treatment in that position was more likely than not the proper treatment" instead of the phrase "realistic possibility of being sustained on its merits" contained therein.

(3) Section 6694(a)(3) of the Internal Revenue Code is modified to substitute the phrase "or there was no reasonable basis for the tax treatment of that position" instead of the phrase "or was frivolous" contained therein.

~~(b)~~

(c) Section 6694(b) of the Internal Revenue Code is modified to substitute "\$5,000" for "\$1,000."

~~(e)~~

(d) Section 6694(c) of the Internal Revenue Code shall not apply and, in lieu thereof, the following shall apply:

(1) If, within 30 days after the day on which notice and demand of any penalty under Section 6694(a) or 6694(b) of the Internal Revenue Code is made against any person who is an income tax return preparer, that person pays an amount which is not less than 15 percent of the amount of that penalty and files a

1 claim for refund of the amount so paid, no levy or proceeding in
2 court for the collection of the remainder of that penalty shall be
3 made, begun, or prosecuted until the final resolution of a
4 proceeding begun as provided in paragraph (2). Notwithstanding
5 Section 19381, the beginning of that proceeding or levy during
6 the time that prohibition is in force may be enjoined in a
7 proceeding in the superior court.

8 (2) If, within 30 days after the day on which a claim for refund
9 of any partial payment of any penalty under Section 6694(a) or
10 6694(b) of the Internal Revenue Code is denied (or, if earlier,
11 within 30 days after the expiration of six months after the day on
12 which the claim for refund has been filed), the income tax return
13 preparer fails to begin a proceeding in the superior court for the
14 determination of his or her liability for that penalty, paragraph (1)
15 shall cease to apply with respect to that penalty, effective on the
16 day following the close of the applicable 30-day period referred
17 to in this subdivision.

18 (3) The running of the period of limitations provided in
19 Section 19371 on the collection by levy or by a proceeding in
20 court in respect of any penalty described in paragraph (1) shall be
21 suspended for the period during which the Franchise Tax Board
22 is prohibited from collecting by levy or a proceeding in court.

23 *SEC. 47.4. Section 19173 of the Revenue and Taxation Code*
24 *is amended to read:*

25 19173. (a) ~~(1) Any person required to register under Section~~
26 ~~18628 or maintain and provide a list under Section 18648, for~~
27 ~~any calendar year, is liable for a penalty, as determined under~~
28 ~~subdivision (b), if that person does any of the following: A~~
29 ~~penalty shall be imposed under this part for failure to maintain~~
30 ~~lists of advisees with respect to reportable transactions and shall~~
31 ~~be determined in accordance with Section 6708 of the Internal~~
32 ~~Revenue Code, except as otherwise provided.~~

33 (A) (i) ~~Fails to register under Section 18628 on or before the~~
34 ~~date prescribed therefor.~~

35 (ii) ~~For reportable transactions (as defined under Section~~
36 ~~18407), fails to furnish the list within 20 days of a request.~~

37 (iii) ~~For listed transactions, fails to provide the list on or before~~
38 ~~the date prescribed therefor in Section 18648.~~

~~(B) Registers a tax shelter or provides a list which fails to show the information required under Section 18628 or Section 18648.~~

~~(C) Fails to furnish the required statement to each investor.~~

~~(2) Paragraph (1) of this subdivision does not apply if it is shown that subdivision (d) applies or that the information required under paragraph (2) of subdivision (b) of Section 18628 was not identified in a Franchise Tax Board notice issued prior to the date the transaction or shelter was entered into.~~

~~(b) (1) (A) For purposes of subdivision (a), the amount determined under this subdivision for a tax shelter required to be registered under Section 18628 is, except as provided in subparagraph (B), fifteen thousand dollars (\$15,000). If a material advisor fails to meet the requirements of subdivision (d) of Section 18648 with respect to a listed transaction, as defined in Section 6707A(c)(2) of the Internal Revenue Code, an additional penalty shall be imposed equal to the greater of:~~

~~(1) One hundred thousand dollars (\$100,000).~~

~~(2) Fifty percent of the gross income that the material advisor derived from that activity.~~

~~(c) A penalty imposed under this section does not apply if it is shown that the additional information required under paragraph (1) of subdivision (d) of Section 18648 was not identified in a Franchise Tax Board notice issued prior to the date the transaction or shelter was entered into.~~

~~(B) If the penalty is with respect to a listed transaction (as defined under Section 18407), the amount determined under this subdivision for a tax shelter required to be registered under Section 18628 shall be the greater of:~~

~~(i) One hundred thousand dollars (\$100,000).~~

~~(ii) Fifty percent of the gross income that the organizer or material advisor derived from that activity.~~

~~(C) In the case of intentional disregard by an organizer or material advisor of the requirement to maintain and provide information regarding a listed transaction (as defined under Section 18407), the percentage of gross income under clause (ii) of subparagraph (B) is "75 percent" instead of "50 percent."~~

~~(2) For purposes of subdivision (a), the amount determined under this subdivision for the failure to provide a list required to be maintained under Section 18648 is as follows:~~

1 ~~(A) For reportable transactions, the penalty amount shall be~~
2 ~~ten thousand dollars (\$10,000) for each day after the 20th day~~
3 ~~that the organizer or material advisor has failed to make the list~~
4 ~~available to the Franchise Tax Board after written request for that~~
5 ~~list was made by the Franchise Tax Board.~~

6 ~~(B) For listed transactions, the penalty amount shall be~~
7 ~~determined under subparagraph (B) of paragraph (1).~~

8 ~~(e)~~

9 ~~(d)~~ The penalty imposed by subdivision (a) shall be assessed
10 ~~against the person required to file a copy of the federal~~
11 ~~registration or required to register under Section 18628, or the~~
12 ~~person required to maintain or provide a list under Section~~
13 ~~18648. The penalty may be assessed at any time during the~~
14 ~~period ending eight years after the failure has occurred.~~

15 ~~(d)~~

16 ~~(e)~~ (1) The Chief Counsel of the Franchise Tax Board may
17 ~~rescind all or any portion of any penalty imposed by subdivision~~
18 ~~(a) this section with respect to any violation with respect to a tax~~
19 ~~shelter required to be registered under Section 18628, or a list~~
20 ~~required to be maintained or provided under Section 18648, if all~~
21 ~~of the following apply:~~

22 (A) The violation is with respect to a reportable transaction,
23 ~~other than a listed transaction (as defined under subdivision (a) of~~
24 ~~Section 18407), as defined in Section 6707A(c)(2) of the Internal~~
25 ~~Revenue Code.~~

26 (B) The person on whom the penalty is imposed has a history
27 of complying with the requirements of this part and Part 10
28 (commencing with Section 17001) or Part 11 (commencing with
29 Section 23001).

30 (C) It is shown that the violation is due to an unintentional
31 mistake of fact.

32 (D) Imposing the penalty would be against equity and good
33 conscience.

34 (E) Rescinding the penalty would promote compliance with
35 the requirements of this part and Part 10 (commencing with
36 Section 17001) or Part 11 (commencing with Section 23001) and
37 effective tax administration.

38 (2) The exercise of authority under paragraph (1) shall be at
39 the sole discretion of the Chief Counsel of the Franchise Tax
40 Board and may not be delegated.

(3) Notwithstanding any other law or rule of law, any determination under this subdivision may not be reviewed in any administrative or judicial proceeding.

(e)

(f) Article 3 (commencing with Section 19031) of this chapter (relating to deficiency assessments) shall not apply with respect to the assessment or collection of any penalty imposed by subdivision (a).

(f)

(g) The penalty imposed by this section is in addition to any penalty imposed under Part 10 (commencing with Section 17001), Part 11 (commencing with Section 23001), or this part.

SEC. 47.5. Section 19177 of the Revenue and Taxation Code is amended to read:

19177. (a) A penalty shall be imposed for promoting abusive tax shelters. The penalty shall be determined in accordance with the provisions of Section 6700 of the Internal Revenue Code, except as otherwise provided.

(b) ~~Notwithstanding Section 6700(a) of the Internal Revenue Code, if an activity with respect to which a penalty imposed under Section 6700(a) of the Internal Revenue Code involves a statement described in Section 6700(a)(2)(A) of the Internal Revenue Code, the amount of the penalty imposed under subdivision (a) shall be equal to 50 percent of the gross income derived (or to be derived) from that activity by the person on which the penalty is imposed.~~

SEC. 47.6. Section 19179 of the Revenue and Taxation Code is amended to read:

19179. A penalty shall be imposed for filing a frivolous return. The penalty shall be determined in accordance with Section 6702 of the Internal Revenue Code, except as otherwise provided.

(a) Section 6702 of the Internal Revenue Code shall be applied to returns required to be filed under this part.

(b) ~~For taxpayers that have been contacted by the Franchise Tax Board regarding the use of a potentially abusive tax shelter (within the meaning of Section 19777), a reportable transaction, as defined in Section 6707A(c)(1) of the Internal Revenue Code with respect to which the requirements of Section 6664(d)(2)(A) of the Internal Revenue Code are not met, any listed transaction,~~

1 *as defined in Section 6707A(c)(2) of the Internal Revenue Code,*
2 *or a gross misstatement within the meaning of Section*
3 *6404(g)(2)(D) of the Internal Revenue Code, Section 6702(a) of*
4 *the Internal Revenue Code is modified as follows:*

5 (1) By substituting “\$5,000” instead of “\$500.”

6 (2) By substituting the term “person” instead of the term
7 “individual” in each place that it appears.

8 (3) By substituting “tax imposed under Part 10 (commencing
9 with Section 17001), Part 11 (commencing with Section 23001),
10 or this part” instead of the phrase “tax imposed by subtitle A”
11 contained therein.

12 (4) By substituting the phrase “is based on” instead of the
13 phrase “is due to” contained therein.

14 (5) By substituting the phrase “frivolous or is based on a
15 position that the Franchise Tax Board has identified as frivolous
16 under subdivision (c) of Section 19179” instead of the term
17 “frivolous” contained therein.

18 (6) By substituting the phrase “reflects a desire to delay or
19 impede the administration of federal income tax laws as
20 determined by the Secretary of the Treasury or the administration
21 of the tax imposed under Part 10 (commencing with Section
22 17001), Part 11 (commencing with Section 23001), or this part as
23 determined by the Franchise Tax Board” instead of the phrase “a
24 desire (which appears on the purported return) to delay or impede
25 the administration of Federal income tax laws” contained therein.

26 (c) (1) The Franchise Tax Board shall prescribe (and
27 periodically revise) a list of positions which the Secretary of the
28 Treasury for federal income tax purposes or the Franchise Tax
29 Board has identified as being frivolous for purposes of this
30 section.

31 (2) Chapter 3.5 (commencing with Section 11340) of Part 1 of
32 Division 3 of Title 2 of the Government Code does not apply to
33 any standard, criterion, procedure, determination, rule, notice, or
34 guideline established or prescribed by the Franchise Tax Board
35 pursuant to paragraph (1).

36 (d) (1) Except as provided in paragraph (3), any person who
37 submits a specified frivolous submission shall pay a penalty of
38 five thousand dollars (\$5,000).

39 (2) For purposes of this section, all of the following shall
40 apply:

1 (A) The phrase “specified frivolous submission” means a
2 specified submission if any portion of that submission meets any
3 of the following conditions:

4 (i) Is based on a position which the Franchise Tax Board has
5 identified as frivolous under subdivision (c).

6 (ii) Reflects a desire to delay or impede the administration of
7 federal income tax laws as determined by the Secretary of the
8 Treasury or the administration of the tax imposed under Part 10
9 (commencing with Section 17001), Part 11 (commencing with
10 Section 23001), or this part as determined by the Franchise Tax
11 Board.

12 (B) The phrase “specified submission” means any of the
13 following:

14 (i) A protest under Section 19041.

15 (ii) A request for a hearing under Section 19044.

16 (iii) An application under any of the following sections:

17 (I) Section 19008 (relating to agreements for payment of tax
18 liability in installments).

19 (II) Section 19443 (relating to compromises).

20 (III) Section 21004 (relating to actions of the Taxpayer Right’s
21 Advocate).

22 (3) If the Franchise Tax Board provides a person with notice
23 that a submission is a specified frivolous submission and the
24 person withdraws that submission within 30 days after the notice,
25 the penalty imposed under paragraph (1) does not apply with
26 respect to that submission.

27 (e) (1) The Chief Counsel of the Franchise Tax Board may
28 rescind all or any portion of any penalty imposed by this section
29 if both of the following apply:

30 (A) Imposing the penalty would be against equity and good
31 conscience.

32 (B) Rescinding the penalty would promote compliance with
33 the requirements of this part and Part 10 (commencing with
34 Section 17001) or Part 11 (commencing with Section 23001) and
35 effective tax administration.

36 (2) The exercise of authority under paragraph (1) shall be at
37 the sole discretion of the Chief Counsel of the Franchise Tax
38 Board and may not be delegated.

1 (3) Notwithstanding any other law or rule of law, any
2 determination under this subdivision may not be reviewed in any
3 administrative or judicial proceeding.

4 (f) The penalties imposed by this section shall be in addition to
5 any other penalty provided by law.

6 *SEC. 47.7. Section 19182 of the Revenue and Taxation Code*
7 *is amended to read:*

8 19182. (a) A penalty shall be imposed for failure to furnish
9 information pursuant to Section 18628 and ~~the penalty amount~~
10 shall be determined in accordance with Section 6707 of the
11 Internal Revenue Code, *relating to failure to furnish information*
12 *regarding reportable transactions, except as otherwise provided.*

13 ~~(b) If the person required to register the tax shelter has~~
14 ~~complied, for federal purposes, with the requirements of Section~~
15 ~~6111(d) of the Internal Revenue Code, relating to certain~~
16 ~~confidential arrangements treated as tax shelters, the person~~
17 ~~required to register the tax shelter is deemed to have complied~~
18 ~~with the requirements of Section 18628 for purposes of this part~~
19 ~~and no penalty shall be imposed under subdivision (a).~~

20 (e)

21 (b) Article 3 (commencing with Section 19031) of this chapter
22 (relating to deficiency assessments) does not apply in respect of
23 the assessment or collection of any penalty imposed under this
24 section.

25 (c) *A penalty under this section does not apply if it is shown*
26 *that the additional information required under paragraph (2) of*
27 *subdivision (d) of Section 18628 was not identified in a*
28 *Franchise Tax Board notice issued prior to the date the*
29 *transaction or shelter was entered into.*

30 (d) *The provisions of subdivision (e) of Section 19183, relating*
31 *to the rescission of the penalty by the Chief Counsel, shall apply*
32 *to any penalty imposed by this section.*

33 *SEC. 48. Section 19184 of the Revenue and Taxation Code is*
34 *amended to read:*

35 19184. (a) A penalty of fifty dollars (\$50) shall be imposed
36 for each failure, unless it is shown that the failure is due to
37 reasonable cause, by any person required to file who fails to file
38 a report at the time and in the manner required by any of the
39 following provisions:

1 (1) Subdivision (c) of Section 17507, relating to individual
2 retirement accounts.

3 (2) Section 220(h) of the Internal Revenue Code, relating to
4 medical savings accounts for taxable years beginning on or after
5 January 1, 1997.

6 (3) Subdivision (b) of Section 17140.3 or subdivision (b) of
7 Section 23711 relating to qualified tuition programs.

8 (4) Subdivision (e) of Section 23712, relating to Coverdell
9 education savings accounts.

10 (5) Section 223(h) of the Internal Revenue Code, relating to
11 health savings accounts.

12 (b) (1) Any individual who:

13 (A) Is required to furnish information under Section 17508 as
14 to the amount designated nondeductible contributions made for
15 any taxable year, and

16 (B) Overstates the amount of those contributions made for that
17 taxable year, shall pay a penalty of one hundred dollars (\$100)
18 for each overstatement unless it is shown that the overstatement
19 is due to reasonable cause.

20 (2) Any individual who fails to file a form required to be filed
21 by the Franchise Tax Board under Section 17508 shall pay a
22 penalty of fifty dollars (\$50) for each failure unless it is shown
23 that the failure is due to reasonable cause.

24 (c) Article 3 (commencing with Section 19031) of this chapter
25 (relating to deficiency assessments) shall not apply in respect of
26 the assessment or collection of any penalty imposed under this
27 section.

28 SEC. 49. Section 19559 of the Revenue and Taxation Code,
29 as added by Section 7 of Chapter 690 of the Statutes of 2002, is
30 repealed.

31 SEC. 50. Section 19559 of the Revenue and Taxation Code,
32 as added by Section 16 of Chapter 807 of the Statutes of 2002, is
33 amended to read:

34 19559. (a) (1) The Franchise Tax Board may disclose
35 returns and return information to federal agencies on the same
36 terms and to the same extent as returns and return information
37 may be disclosed by the Secretary of the Treasury under
38 paragraph (3)(C) or paragraph (7) of Section 6103(i) of the
39 Internal Revenue Code.

(2) Notwithstanding paragraph (1), the Franchise Tax Board may not disclose any return or return information under this section if the Franchise Tax Board determines, in the manner specified by the Franchise Tax Board, that this disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

(b) This section shall apply to disclosures made on or after January 23, 2002, except that no disclosures may be made under this section after December 31, 2005.

SEC. 50.1. Section 19772 of the Revenue and Taxation Code, as added by Section 13 of Chapter 656 of the Statutes of 2003, is amended to read:

~~19772. (a) Any large entity or high net worth individual who fails to include on any return or statement any information with respect to a reportable transaction that is required under Section 6011 of the Internal Revenue Code, as modified by Section 18407, to be included with that return or statement shall pay a penalty for each omission in the amount determined under subdivision (b).~~ *Section 6707A of the Internal Revenue Code, relating to penalty for failure to include reportable transactions information with a return, shall apply, except as otherwise provided.*

~~(b) (1) Except~~ *The penalty amounts in Section 6707A(b) of the Internal Revenue Code shall not apply, and in lieu thereof, the following shall apply:*

(1) Except as provided in paragraph (2), the amount of the penalty under subdivision (a) shall be fifteen thousand dollars (\$15,000).

(2) The amount of the penalty under subdivision (a) with respect to a listed transaction shall be thirty thousand dollars (\$30,000).

~~(c) For purposes of this section:~~ *(1) Section 6707A(c)(1) of the Internal Revenue Code is modified to include reportable transactions within the meaning of paragraph (3) of subdivision (a) of Section 18407.*

~~(1) The term "high net worth individual" means, with respect to a transaction, an individual whose net worth exceeds two million dollars (\$2,000,000) immediately before the transaction.~~

~~(2) The term "large entity" means, with respect to any taxable year, a person (other than an individual) with gross receipts in~~

1 excess of ten million dollars (\$10,000,000) for either the taxable
2 year in which the reportable transaction occurs or in the
3 preceding taxable year. Rules similar to the rules of Section
4 448(e)(2) and 448(e)(3) of the Internal Revenue Code, other than
5 Section 448(e)(3)(A) of the Internal Revenue Code, shall apply
6 for purposes of this paragraph.

7 (d) For purposes of this section:

8 (1) The term “reportable transaction” means any transaction
9 with respect to which information is required to be included with
10 a return or statement because, as determined under regulations
11 prescribed by the Secretary of the Treasury under Section 6011
12 of the Internal Revenue Code for federal income tax purposes or
13 by the Franchise Tax Board under Section 18407, that transaction
14 is of a type that the Secretary of the Treasury for federal income
15 tax purposes or the Franchise Tax Board determines as having a
16 potential for tax avoidance or evasion.

17 (2) Except as provided in regulations prescribed by the
18 Secretary of the Treasury or by the Franchise Tax Board, the
19 term “listed transaction” means a reportable transaction (as
20 defined in paragraph (1)) that is the same as, or substantially
21 similar to, a transaction specifically identified by the Secretary of
22 the Treasury for purposes of Section 6011 of the Internal
23 Revenue Code for federal income tax purposes or by the
24 Franchise Tax Board for purposes of Section 6011 of the Internal
25 Revenue Code or Section 18407, as a tax avoidance transaction.

26 (e) (1) The

27 (2) Section 6707A(c)(2) of the Internal Revenue Code is
28 modified to include listed transactions within the meaning of
29 paragraph (4) of subdivision (a) of Section 18407.

30 (d) The penalty under this section only applies to taxpayers
31 with taxable income greater than two hundred thousand dollars
32 (\$200,000).

33 (e) Section 6707A(e) of the Internal Revenue Code, relating to
34 a penalty reported to the Securities and Exchange Commission,
35 shall not apply.

36 (f) Section 6707A(d) of the Internal Revenue Code, relating to
37 the authority to rescind a penalty, shall not apply, and in lieu
38 thereof, the following shall apply:

1 (1) The Chief Counsel of the Franchise Tax Board may rescind
2 all or any portion of any penalty imposed by this section with
3 respect to any violation if all of the following apply:

4 (A) The violation is with respect to a reportable transaction
5 other than a listed transaction.

6 (B) The person on whom the penalty is imposed has a history
7 of complying with the requirements of this part and Part 10
8 (commencing with Section 17001) or Part 11 (commencing with
9 Section 23001).

10 (C) It is shown that the violation is due to an unintentional
11 mistake of fact.

12 (D) Imposing the penalty would be against equity and good
13 conscience.

14 (E) Rescinding the penalty would promote compliance with
15 the requirements of this part and Part 10 (commencing with
16 Section 17001) or Part 11 (commencing with Section 23001) and
17 effective tax administration.

18 (2) The exercise of authority under paragraph (1) shall be at
19 the sole discretion of the Chief Counsel of the Franchise Tax
20 Board and may not be delegated.

21 (3) Notwithstanding any other law or rule of law, any
22 determination under this subdivision may not be reviewed in any
23 administrative or judicial proceeding.

24 ~~(f)~~

25 (g) Article 3 (commencing with Section 19031) of Chapter 4
26 (relating to deficiency assessments) shall not apply with respect
27 to the assessment or collection of any penalty imposed under this
28 section.

29 ~~(g)~~

30 (h) The penalty imposed by this section is in addition to any
31 penalty imposed under Part 10 (commencing with Section
32 17001), Part 11 (commencing with Section 23001), or this part.

33 *SEC. 50.2. Section 19772 of the Revenue and Taxation Code,*
34 *as added by Section 13 of Chapter 654 of the Statutes of 2003, is*
35 *repealed.*

36 ~~19772. (a) Any large entity or high net worth individual who~~
37 ~~fails to include on any return or statement any information with~~
38 ~~respect to a reportable transaction that is required under Section~~
39 ~~6011 of the Internal Revenue Code, as modified by Section~~
40 ~~18407, to be included with that return or statement shall pay a~~

1 ~~penalty for each omission in the amount determined under~~
2 ~~subdivision (b).~~

3 ~~(b) (1) Except as provided in paragraph (2), the amount of the~~
4 ~~penalty under subdivision (a) shall be fifteen thousand dollars~~
5 ~~(\$15,000).~~

6 ~~(2) The amount of the penalty under subdivision (a) with~~
7 ~~respect to a listed transaction shall be thirty thousand dollars~~
8 ~~(\$30,000).~~

9 ~~(c) For purposes of this section:~~

10 ~~(1) The term “high net worth individual” means, with respect~~
11 ~~to a transaction, an individual whose net worth exceeds two~~
12 ~~million dollars (\$2,000,000) immediately before the transaction.~~

13 ~~(2) The term “large entity” means, with respect to any taxable~~
14 ~~year, a person (other than an individual) with gross receipts in~~
15 ~~excess of ten million dollars (\$10,000,000) for either the taxable~~
16 ~~year in which the reportable transaction occurs or in the~~
17 ~~preceding taxable year. Rules similar to the rules of Section~~
18 ~~448(e)(2) and 448(e)(3) of the Internal Revenue Code, other than~~
19 ~~Section 448(e)(3)(A) of the Internal Revenue Code, shall apply~~
20 ~~for purposes of this paragraph.~~

21 ~~(d) For purposes of this section:~~

22 ~~(1) The term “reportable transaction” means any transaction~~
23 ~~with respect to which information is required to be included with~~
24 ~~a return or statement because, as determined under regulations~~
25 ~~prescribed by the Secretary of the Treasury under Section 6011~~
26 ~~of the Internal Revenue Code for federal income tax purposes or~~
27 ~~by the Franchise Tax Board under Section 18407, that transaction~~
28 ~~is of a type that the Secretary of the Treasury for federal income~~
29 ~~tax purposes or the Franchise Tax Board determines as having a~~
30 ~~potential for tax avoidance or evasion.~~

31 ~~(2) Except as provided in regulations prescribed by the~~
32 ~~Secretary of the Treasury or by the Franchise Tax Board, the~~
33 ~~term “listed transaction” means a reportable transaction (as~~
34 ~~defined in paragraph (1)) that is the same as, or substantially~~
35 ~~similar to, a transaction specifically identified by the Secretary of~~
36 ~~the Treasury for purposes of Section 6011 of the Internal~~
37 ~~Revenue Code for federal income tax purposes or by the~~
38 ~~Franchise Tax Board for purposes of Section 6011 of the Internal~~
39 ~~Revenue Code or Section 18407, as a tax avoidance transaction.~~

~~(e) (1) The Chief Counsel of the Franchise Tax Board may rescind all or any portion of any penalty imposed by this section with respect to any violation if all of the following apply:~~

~~(A) The violation is with respect to a reportable transaction other than a listed transaction.~~

~~(B) The person on whom the penalty is imposed has a history of complying with the requirements of this part and Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001).~~

~~(C) It is shown that the violation is due to an unintentional mistake of fact.~~

~~(D) Imposing the penalty would be against equity and good conscience.~~

~~(E) Rescinding the penalty would promote compliance with the requirements of this part and Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001) and effective tax administration.~~

~~(2) The exercise of authority under paragraph (1) shall be at the sole discretion of the Chief Counsel of the Franchise Tax Board and may not be delegated.~~

~~(3) Notwithstanding any other law or rule of law, any determination under this subdivision may not be reviewed in any administrative or judicial proceeding.~~

~~(f) Article 3 (commencing with Section 19031) of Chapter 4 (relating to deficiency assessments) shall not apply with respect to the assessment or collection of any penalty imposed under this section.~~

~~(g) The penalty imposed by this section is in addition to any penalty imposed under Part 10 (commencing with Section 17001), Part 11 (commencing with Section 23001), or this part.~~

SEC. 50.3. Section 19773 of the Revenue and Taxation Code, as added by Section 13 of Chapter 656 of the Statutes of 2003, is repealed.

~~19773. (a) If a taxpayer has a reportable transaction understatement for any taxable year, there shall be added to the tax an amount equal to 20 percent of the amount of that understatement.~~

~~(b) For purposes of this section, both of the following shall apply:~~

~~(1) The term “reportable transaction understatement” means the sum of subparagraphs (A) and (B):~~

~~(A) The product of:~~

~~(i) The amount of the increase (if any) in taxable income which results from a difference between the proper tax treatment of an item to which this section applies and the taxpayer’s treatment of that item (as shown on the taxpayer’s return of tax):~~

~~(ii) The highest rate of tax imposed on the taxpayer under Part 10 (commencing with Section 17001) in the case of a taxpayer subject to tax under that part or under Part 11 (commencing with Section 23001) in the case of a taxpayer that is subject to tax under that part.~~

~~(B) The amount of the decrease (if any) in the aggregate amount of credits determined under Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001), as applicable, that results from a difference between the taxpayer’s treatment of an item to which this section applies (as shown on the taxpayer’s return of tax) and the proper tax treatment of that item.~~

~~(C) For purposes of subparagraph (A), any reduction of the excess of deductions allowed for the taxable year over gross income for that year, and any reduction in the amount of capital losses which would (without regard to Section 1211 of the Internal Revenue Code) be allowed for that year, shall be treated as an increase in taxable income.~~

~~(2) This section shall apply to any item that is attributable to either of the following:~~

~~(A) Any listed transaction.~~

~~(B) Any reportable transaction (other than a listed transaction) if a significant purpose of that transaction is the avoidance or evasion of tax imposed under Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001):~~

~~(c) (1) Subdivision (a) shall be applied by substituting “30 percent” for “20 percent” with respect to the portion of any reportable transaction understatement with respect to which the requirement of Section 6664 of the Internal Revenue Code, as modified by subparagraph (A) of paragraph (2) of subdivision (d) of Section 19164, is not met.~~

~~(2) (A) If the notice of proposed assessment of additional tax has been sent with respect to a penalty to which this section~~

1 applies, only the Chief Counsel of the Franchise Tax Board may
2 compromise all or any portion of that penalty.

3 (B) The exercise of authority under subparagraph (A) shall be
4 at the sole discretion of the Chief Counsel of the Franchise Tax
5 Board and may not be delegated.

6 (C) Notwithstanding any other law or rule of law, any
7 determination under this subdivision may not be reviewed in any
8 administrative or judicial proceeding.

9 (d) For purposes of this section, the terms “reportable
10 transaction” and “listed transaction” have the respective
11 meanings given to those terms by subdivision (a) of Section
12 18407.

13 (e) (1) In the case of an understatement (as defined in Section
14 6662(d)(2) of the Internal Revenue Code) all of the following
15 shall apply:

16 (A) The amount of the understatement (determined without
17 regard to this paragraph) shall be increased by the aggregate
18 amount of reportable transaction understatements and
19 noneconomic substance transaction understatements for purposes
20 of determining whether the understatement is a substantial
21 understatement under Section 6662(d)(1) of the Internal Revenue
22 Code.

23 (B) The addition to tax under subdivision (a) of Section 19164
24 shall apply only to the excess of the amount of the substantial
25 understatement (if any) after the application of subparagraph (A)
26 over the aggregate amount of reportable transaction
27 understatements and noneconomic substance transaction
28 understatements.

29 (2) (A) In determining the fraud penalty imposed under
30 subdivision (c) of Section 19164, references to an underpayment
31 in Section 6663 of the Internal Revenue Code shall be treated as
32 including references to a reportable transaction understatement
33 and a noneconomic substance transaction understatement.

34 (B) This section does not apply to any portion of an
35 understatement on which a penalty is imposed under Section
36 19774.

37 (3) Except as provided in regulations, in no event may any tax
38 treatment included with an amendment or supplement to a return
39 of tax be taken into account in determining the amount of any
40 reportable transaction understatement or noneconomic substance

1 ~~transaction understatement, if the amendment or supplement is~~
2 ~~filed after the earlier of the date the taxpayer is first contacted by~~
3 ~~either the Secretary of the Treasury for federal income tax~~
4 ~~purposes or the Franchise Tax Board regarding the examination~~
5 ~~of the return or such other date as is specified by the Franchise~~
6 ~~Tax Board.~~

7 ~~(4) For purposes of this subdivision, the term “noneconomic~~
8 ~~substance transaction understatement” has the meaning given that~~
9 ~~term by subdivision (c) of Section 19774.~~

10 *SEC. 50.4. Section 19773 of the Revenue and Taxation Code,*
11 *as added by Section 13 of Chapter 654 of the Statutes of 2003, is*
12 *repealed.*

13 ~~19773. (a) If a taxpayer has a reportable transaction~~
14 ~~understatement for any taxable year, there shall be added to the~~
15 ~~tax an amount equal to 20 percent of the amount of that~~
16 ~~understatement.~~

17 ~~(b) For purposes of this section, both of the following shall~~
18 ~~apply:~~

19 ~~(1) The term “reportable transaction understatement” means~~
20 ~~the sum of subparagraphs (A) and (B):~~

21 ~~(A) The product of:~~

22 ~~(i) The amount of the increase (if any) in taxable income~~
23 ~~which results from a difference between the proper tax treatment~~
24 ~~of an item to which this section applies and the taxpayer’s~~
25 ~~treatment of that item (as shown on the taxpayer’s return of tax):~~

26 ~~(ii) The highest rate of tax imposed on the taxpayer under Part~~
27 ~~10 (commencing with Section 17001) in the case of a taxpayer~~
28 ~~subject to tax under that part or under Part 11 (commencing with~~
29 ~~Section 23001) in the case of a taxpayer that is subject to tax~~
30 ~~under that part.~~

31 ~~(B) The amount of the decrease (if any) in the aggregate~~
32 ~~amount of credits determined under Part 10 (commencing with~~
33 ~~Section 17001) or Part 11 (commencing with Section 23001), as~~
34 ~~applicable, that results from a difference between the taxpayer’s~~
35 ~~treatment of an item to which this section applies (as shown on~~
36 ~~the taxpayer’s return of tax) and the proper tax treatment of that~~
37 ~~item.~~

38 ~~(C) For purposes of subparagraph (A), any reduction of the~~
39 ~~excess of deductions allowed for the taxable year over gross~~
40 ~~income for that year, and any reduction in the amount of capital~~

1 losses which would (without regard to Section 1211 of the
2 Internal Revenue Code) be allowed for that year, shall be treated
3 as an increase in taxable income.

4 (2) This section shall apply to any item that is attributable to
5 either of the following:

6 (A) Any listed transaction.

7 (B) Any reportable transaction (other than a listed transaction)
8 if a significant purpose of that transaction is the avoidance or
9 evasion of tax imposed under Part 10 (commencing with Section
10 17001) or Part 11 (commencing with Section 23001).

11 (e) (1) Subdivision (a) shall be applied by substituting “30
12 percent” for “20 percent” with respect to the portion of any
13 reportable transaction understatement with respect to which the
14 requirement of Section 6664 of the Internal Revenue Code, as
15 modified by subparagraph (A) of paragraph (2) of subdivision (d)
16 of Section 19164, is not met.

17 (2) (A) If the notice of proposed assessment of additional tax
18 has been sent with respect to a penalty to which this section
19 applies, only the Chief Counsel of the Franchise Tax Board may
20 compromise all or any portion of that penalty.

21 (B) The exercise of authority under subparagraph (A) shall be
22 at the sole discretion of the Chief Counsel of the Franchise Tax
23 Board and may not be delegated.

24 (C) Notwithstanding any other law or rule of law, any
25 determination under this subdivision may not be reviewed in any
26 administrative or judicial proceeding.

27 (d) For purposes of this section, the terms “reportable
28 transaction” and “listed transaction” have the respective
29 meanings given to those terms by subdivision (a) of Section
30 18407.

31 (e) (1) In the case of an understatement (as defined in Section
32 6662(d)(2) of the Internal Revenue Code) all of the following
33 shall apply:

34 (A) The amount of the understatement (determined without
35 regard to this paragraph) shall be increased by the aggregate
36 amount of reportable transaction understatements and
37 noneconomic substance transaction understatements for purposes
38 of determining whether the understatement is a substantial
39 understatement under Section 6662(d)(1) of the Internal Revenue
40 Code.

~~(B) The addition to tax under subdivision (a) of Section 19164 shall apply only to the excess of the amount of the substantial understatement (if any) after the application of subparagraph (A) over the aggregate amount of reportable transaction understatements and noneconomic substance transaction understatements.~~

~~(2) (A) In determining the fraud penalty imposed under subdivision (c) of Section 19164, references to an underpayment in Section 6663 of the Internal Revenue Code shall be treated as including references to a reportable transaction understatement and a noneconomic substance transaction understatement.~~

~~(B) This section does not apply to any portion of an understatement on which a penalty is imposed under Section 19774.~~

~~(3) Except as provided in regulations, in no event may any tax treatment included with an amendment or supplement to a return of tax be taken into account in determining the amount of any reportable transaction understatement or noneconomic substance transaction understatement, if the amendment or supplement is filed after the earlier of the date the taxpayer is first contacted by either the Secretary of the Treasury for federal income tax purposes or the Franchise Tax Board regarding the examination of the return or such other date as is specified by the Franchise Tax Board.~~

~~(4) For purposes of this subdivision, the term “noneconomic substance transaction understatement” has the meaning given that term by subdivision (c) of Section 19774.~~

SEC. 50.5. Section 19774 of the Revenue and Taxation Code, as added by Section 13 of Chapter 656 of the Statutes of 2003, is amended to read:

19774. (a) If a taxpayer has a noneconomic substance transaction understatement for any taxable year, there shall be added to the tax an amount equal to 40 percent of the amount of that understatement.

(b) (1) Subdivision (a) shall be applied by substituting “20 percent” for “40 percent” with respect to the portion of any noneconomic substance transaction understatement with respect to which the relevant facts affecting the tax treatment of the item are adequately disclosed in the return or a statement attached to the return.

(2) For taxable years beginning before January 1, 2003, “adequately disclosed” includes the disclosure of the tax shelter identification number on the taxpayer’s return as required by subdivision (c) of Section 18628, *as applicable for the year in which the transaction was entered into.*

(c) For purposes of this section:

(1) The term “noneconomic substance transaction understatement” means any amount which would be an understatement under ~~paragraph (1) of Section 6662A(b) of the Internal Revenue Code, as modified by subdivision (b) of Section 19773 19164.5~~ if ~~Section 19773 6662A(b) of the Internal Revenue Code~~ were applied by taking into account items attributable to noneconomic substance transactions rather than items to which ~~Section 19773 6662A(b)~~ applies.

(2) A “noneconomic substance transaction” includes the disallowance of any loss, deduction or credit, or addition to income attributable to a determination that the disallowance or addition is attributable to a transaction or arrangement that lacks economic substance including a transaction or arrangement in which an entity is disregarded as lacking economic substance. A transaction shall be treated as lacking economic substance if the taxpayer does not have a valid nontax California business purpose for entering into the transaction.

(d) (1) If the notice of proposed assessment of additional tax has been sent with respect to a penalty to which this section applies, only the Chief Counsel of the Franchise Tax Board may compromise all or any portion of that penalty.

(2) The exercise of authority under paragraph (1) shall be at the sole discretion of the Chief Counsel of the Franchise Tax Board and may not be delegated.

(3) Notwithstanding any other law or rule of law, any determination under this subdivision may not be reviewed in any administrative or judicial proceeding.

SEC. 50.6. Section 19774 of the Revenue and Taxation Code, as added by Section 13 of Chapter 654 of the Statutes of 2003, is repealed.

~~19774. (a) If a taxpayer has a noneconomic substance transaction understatement for any taxable year, there shall be added to the tax an amount equal to 40 percent of the amount of that understatement.~~

1 ~~(b) (1) Subdivision (a) shall be applied by substituting “20~~
2 ~~percent” for “40 percent” with respect to the portion of any~~
3 ~~noneconomic substance transaction understatement with respect~~
4 ~~to which the relevant facts affecting the tax treatment of the item~~
5 ~~are adequately disclosed in the return or a statement attached to~~
6 ~~the return.~~

7 ~~(2) For taxable years beginning before January 1, 2003,~~
8 ~~“adequately disclosed” includes the disclosure of the tax shelter~~
9 ~~identification number on the taxpayer’s return as required by~~
10 ~~subdivision (c) of Section 18628.~~

11 ~~(e) For purposes of this section:~~

12 ~~(1) The term “noneconomic substance transaction~~
13 ~~understatement” means any amount which would be an~~
14 ~~understatement under paragraph (1) of subdivision (b) of Section~~
15 ~~19773 if Section 19773 were applied by taking into account~~
16 ~~items attributable to noneconomic substance transactions rather~~
17 ~~than items to which Section 19773 applies.~~

18 ~~(2) A “noneconomic substance transaction” includes the~~
19 ~~disallowance of any loss, deduction or credit, or addition to~~
20 ~~income attributable to a determination that the disallowance or~~
21 ~~addition is attributable to a transaction or arrangement that lacks~~
22 ~~economic substance including a transaction or arrangement in~~
23 ~~which an entity is disregarded as lacking economic substance. A~~
24 ~~transaction shall be treated as lacking economic substance if the~~
25 ~~taxpayer does not have a valid nontax California business~~
26 ~~purpose for entering into the transaction.~~

27 ~~(d) (1) If the notice of proposed assessment of additional tax~~
28 ~~has been sent with respect to a penalty to which this section~~
29 ~~applies, only the Chief Counsel of the Franchise Tax Board may~~
30 ~~compromise all or any portion of that penalty.~~

31 ~~(2) The exercise of authority under paragraph (1) shall be at~~
32 ~~the sole discretion of the Chief Counsel of the Franchise Tax~~
33 ~~Board and may not be delegated.~~

34 ~~(3) Notwithstanding any other law or rule of law, any~~
35 ~~determination under this subdivision may not be reviewed in any~~
36 ~~administrative or judicial proceeding.~~

37 ~~SEC. 50.7. Section 19777 of the Revenue and Taxation Code,~~
38 ~~as amended by Section 331 of Chapter 183 of the Statutes of~~
39 ~~2004, is amended to read:~~

19777. (a) If a taxpayer has been contacted by the Franchise Tax Board regarding the use of a potentially abusive tax shelter, a reportable transaction, as defined in Section 6707A(c)(1) of the Internal Revenue Code with respect to which the requirements of Section 6664(d)(2)(A) of the Internal Revenue Code are not met, any listed transaction, as defined in Section 6707A(c)(2) of the Internal Revenue Code, or a gross misstatement within the meaning of Section 6404(g)(2)(D) of the Internal Revenue Code, and has a deficiency, there shall be added to the tax an amount equal to 100 percent of the interest payable under Section 19101 for the period beginning on the last date prescribed by law for the payment of that tax (determined without regard to extensions) and ending on the date the notice of proposed assessment is mailed.

(b) “Potentially abusive tax shelter” means:

(1) Any tax shelter (as defined in Section 6111 of the Internal Revenue Code) with respect to which registration is required under Section 6111 of the Internal Revenue Code.

(2) Any entity, investment plan or arrangement, or other plan or arrangement which is of a type that the Secretary of the Treasury or the Franchise Tax Board determines by regulations as having a potential for tax avoidance or evasion.

(c)

(b) The penalty imposed by this section is in addition to any other penalty imposed under Part 10 (commencing with Section 17001), Part 11 (commencing with Section 23001), or this part.

(d) This section shall apply to notices of proposed assessments mailed after the effective date of the act adding this section.

SEC. 50.8. Section 19777 of the Revenue and Taxation Code, as amended by Section 330 of Chapter 183 of the Statutes of 2004, is repealed.

19777. (a) If a taxpayer has been contacted by the Franchise Tax Board regarding the use of a potentially abusive tax shelter, and has a deficiency, there shall be added to the tax an amount equal to 100 percent of the interest payable under Section 19101 for the period beginning on the last date prescribed by law for the payment of that tax (determined without regard to extensions) and ending on the date the notice of proposed assessment is mailed.

(b) “Potentially abusive tax shelter” means:

~~(1) Any tax shelter (as defined in Section 6111 of the Internal Revenue Code) with respect to which registration is required under Section 6111 of the Internal Revenue Code.~~

~~(2) Any entity, investment plan or arrangement, or other plan or arrangement which is of a type that the Secretary of the Treasury or the Franchise Tax Board determines by regulations as having a potential for tax avoidance or evasion.~~

~~(e) The penalty imposed by this section is in addition to any other penalty imposed under Part 10 (commencing with Section 17001), Part 11 (commencing with Section 23001), or this part.~~

~~(d) This section shall apply to notices of proposed assessments mailed after the effective date of the act adding this section.~~

SEC. 51. Section 23051.5 of the Revenue and Taxation Code is amended to read:

23051.5. (a) (1) Unless otherwise specifically provided, the terms "Internal Revenue Code," "Internal Revenue Code of 1954," or "Internal Revenue Code of 1986," for purposes of this part, mean Title 26 of the United States Code, including all amendments thereto, as enacted on the specified date for the applicable taxable year as defined in paragraph (1) of subdivision (a) of Section 17024.5.

(2) (A) ~~Unless otherwise specifically provided, for~~ *provided* for federal laws enacted on or after January 1, 1987, and on or before the specified date for the taxable year, uncodified provisions that relate to provisions of the Internal Revenue Code that are incorporated for purposes of this part, shall be applicable to the same taxable years as the incorporated provisions.

(B) In the case where Section 901 of the Economic Growth and Tax Relief Act of 2001 (Public Law 107-16) applies to any provision of the Internal Revenue Code that is incorporated for purposes of this part, Section 901 of the Economic Growth and Tax Relief Act of 2001 (Public Law 107-16) shall apply for purposes of this part in the same manner and to the same taxable years as it applies for federal income tax purposes.

(3) Subtitle G (Tax Technical Corrections) and Part I of Subtitle H (Repeal of Expired or Obsolete Provisions) of the Revenue Reconciliation Act of 1990 (Public Law 101-508) modified numerous provisions of the Internal Revenue Code and provisions of prior federal acts, some of which are incorporated by reference into this part. Unless otherwise provided, the

1 provisions described in the preceding sentence, to the extent that
2 they modify provisions that are incorporated into this part, are
3 declaratory of existing law and shall be applied in the same
4 manner and for the same periods as specified in the Revenue
5 Reconciliation Act of 1990.

6 (b) Unless otherwise specifically provided, when applying the
7 Internal Revenue Code for purposes of this part, a reference to
8 any of the following is not applicable for purposes of this part:

9 (1) Domestic International Sales Corporations (DISC), as
10 defined in Section 992(a) of the Internal Revenue Code.

11 (2) Foreign Sales Corporations (FSC), as defined in Section
12 922(a) of the Internal Revenue Code.

13 (3) A personal holding company, as defined in Section 542 of
14 the Internal Revenue Code.

15 (4) A foreign personal holding company, as defined in Section
16 552 of the Internal Revenue Code.

17 (5) A foreign investment company, as defined in Section
18 1246(b) of the Internal Revenue Code.

19 (6) A foreign trust as defined in Section 679 of the Internal
20 Revenue Code.

21 (7) Foreign income taxes and foreign income tax credits.

22 (8) Federal tax credits and carryovers of federal tax credits.

23 (c) (1) The provisions contained in Sections 41 to 44,
24 inclusive, and Section 172 of the Tax Reform Act of 1984
25 (Public Law 98-369), relating to treatment of debt instruments, is
26 not applicable for taxable years beginning before January 1,
27 1987.

28 (2) The provisions contained in Public Law 99-121, relating to
29 the treatment of debt instruments, is not applicable for taxable
30 years beginning before January 1, 1987.

31 (3) For taxable years beginning on and after January 1, 1987,
32 the provisions referred to by paragraphs (1) and (2) shall be
33 applicable for purposes of this part in the same manner and with
34 respect to the same obligations as the federal provisions, except
35 as otherwise provided in this part.

36 (d) When applying the Internal Revenue Code for purposes of
37 this part, regulations promulgated in final form or issued as
38 temporary regulations by “the secretary” shall be applicable as
39 regulations issued under this part to the extent that they do not

1 conflict with this part or with regulations issued by the Franchise
2 Tax Board.

3 (e) Whenever this part allows a taxpayer to make an election,
4 the following rules shall apply:

5 (1) A proper election filed with the Internal Revenue Service
6 in accordance with the Internal Revenue Code or regulations
7 issued by “the secretary” shall be deemed to be a proper election
8 for purposes of this part, unless otherwise expressly provided in
9 this part or in regulations issued by the Franchise Tax Board.

10 (2) A copy of that election shall be furnished to the Franchise
11 Tax Board upon request.

12 (3) (A) Except as provided in subparagraph (B), in order to
13 obtain treatment other than that elected for federal purposes, a
14 separate election shall be filed with the Franchise Tax Board at
15 the time and in the manner that may be required by the Franchise
16 Tax Board.

17 (B) (i) If a taxpayer makes a proper election for federal
18 income tax purposes prior to the time that taxpayer becomes
19 subject to the tax imposed under this part or Part 10
20 (commencing with Section 17001), that taxpayer is deemed to
21 have made the same election for purposes of the tax imposed by
22 this part, Part 10 (commencing with Section 17001), and Part
23 10.2 (commencing with Section 18401), as applicable, and that
24 taxpayer may not make a separate election for California tax
25 purposes unless that separate election is expressly authorized by
26 this part, Part 10 (commencing with Section 17001), or Part 10.2
27 (commencing with Section 18401), or by regulations issued by
28 the Franchise Tax Board.

29 (ii) If a taxpayer has not made a proper election for federal
30 income tax purposes prior to the time that taxpayer becomes
31 subject to tax under this part or Part 10 (commencing with
32 Section 17001), that taxpayer may not make a separate California
33 election for purposes of this part, Part 10 (commencing with
34 Section 17001), or Part 10.2 (commencing with Section 18401),
35 unless that separate election is expressly authorized by this part,
36 Part 10 (commencing with Section 17001), Part 10.2
37 (commencing with Section 18401), or by regulations issued by
38 the Franchise Tax Board.

39 (iii) This subparagraph applies only to the extent that the
40 provisions of the Internal Revenue Code or regulations issued by

1 “the secretary” authorizing an election for federal income tax
2 purposes apply for purposes of this part, Part 10 (commencing
3 with Section 17001), or Part 10.2 (commencing with Section
4 18401).

5 (f) Whenever this part allows or requires a taxpayer to file an
6 application or seek consent, the rules set forth in subdivision (e)
7 shall apply to that application or consent.

8 (g) When applying the Internal Revenue Code for purposes of
9 determining the statute of limitations under this part, any
10 reference to a period of three years shall be modified to read four
11 years for purposes of this part.

12 (h) When applying, for purposes of this part, any section of the
13 Internal Revenue Code or any applicable regulation thereunder,
14 all of the following shall apply:

15 (1) For purposes of Chapter 2 (commencing with Section
16 23101), Chapter 2.5 (commencing with Section 23400), and
17 Chapter 3 (commencing with Section 23501), the term “taxable
18 income” shall mean “net income.”

19 (2) For purposes of Article 2 (commencing with Section
20 23731) of Chapter 4, the term “taxable income” shall mean
21 “unrelated business taxable income,” as defined by Section
22 23732.

23 (3) Any reference to “subtitle,” “Chapter 1,” or “chapter” shall
24 mean this part.

25 (4) The provisions of Section 7806 of the Internal Revenue
26 Code, relating to construction of title, shall apply.

27 (5) Any provision of the Internal Revenue Code that becomes
28 operative on or after the specified date for that taxable year shall
29 become operative on the same date for purposes of this part.

30 (6) Any provision of the Internal Revenue Code that becomes
31 inoperative on or after the specified date for that taxable year
32 shall become inoperative on the same date for purposes of this
33 part.

34 (7) Due account shall be made for differences in federal and
35 state terminology, effective dates, substitution of “Franchise Tax
36 Board” for “secretary” when appropriate, and other obvious
37 differences.

38 (8) Any provision of the Internal Revenue Code that refers to
39 a “corporation” shall, when applicable for purposes of this part,
40 include a “bank,” as defined by Section 23039.

1 (i) Any reference to a specific provision of the Internal
2 Revenue Code shall include modifications of that provision, if
3 any, in this part.

4 SEC. 52. Section 23662 is added to the Revenue and
5 Taxation Code, to read:

6 23662. (a) For each taxable year beginning on or after
7 ~~January 1, 2006, and before January 1, 2012~~ *July 1, 2005, and*
8 *before January 1, 2018*, there shall be allowed as an
9 environmental tax credit against the “tax,” as defined by Section
10 23036, an amount equal to five cents (\$0.05) for each gallon of
11 ~~ultra-low~~ *ultra low* sulfur diesel fuel produced during the taxable
12 year by a small refiner at any facility located in this state.

13 (b) The aggregate credit determined under subdivision (a) for
14 any taxable year with respect to any facility shall not exceed 25
15 percent of the qualified capital costs incurred by the small refiner
16 with respect to that facility, reduced by the aggregate credits
17 determined under this section for all prior taxable years with
18 respect to that facility.

19 (c) For purposes of this section:

20 (1) “Small refiner” means any refiner who owns or operates a
21 refinery in California that:

22 (A) Has and at all times had since January 1, 1978, a crude oil
23 capacity of not more than 55,000 barrels per stream day.

24 (B) Has not been at any time since September 1, 1988, owned
25 or controlled by any refiner that at the same time owned or
26 controlled refineries in California with a total combined crude oil
27 capacity of more than 55,000 barrels per stream day.

28 (C) Has not been at any time since September 1, 1988, owned
29 or controlled by any refiner that at the same time owned or
30 controlled refineries in the United States with a total combined
31 crude oil capacity of more than 137,500 barrels per stream day.

32 (2) (A) “Qualified capital costs” means, with respect to any
33 facility, those costs paid or incurred during the applicable period
34 for items certified by the California Air Resources Board (*CARB*)
35 under subparagraph (B) for compliance with the applicable EPA
36 or CARB regulations with respect to that facility, including, but
37 not limited to, expenditures for the construction of new process
38 operation units or the dismantling and reconstruction of existing
39 process units to be used in the production of ~~ultra-low~~ *ultra low*
40 sulfur diesel fuel, associated adjacent or offsite equipment

(including tankage, catalyst, and power supply), engineering, construction period interest, site work, and permitting.

(B) (i) Before claiming a credit under this section, a small refiner shall request from the California Air Resources Board a certification that both of the following are true:

(I) That the items for which qualified capital costs were paid or incurred are for compliance with the applicable EPA or CARB regulations described in subparagraph (A).

(II) That the items for which qualified capital costs were paid or incurred have been placed in service by the small refiner.

(ii) The request described in clause (i) shall be in a form and contain sufficient information to allow the California Air Resources Board to determine that the items that are requested to be certified were placed in service for compliance with applicable EPA and CARB regulations, which information shall include the date on which the items were placed in service.

(C) The California Air Resources Board shall make a determination regarding a request described in subparagraph (B) on or before 60 days after the request is submitted. If the board does not make a determination within this time period, the certification will be deemed to be granted.

(D) If certification from the Secretary of the Treasury of the United States, after consultation with the Administrator of the Environmental Protection Agency, that the taxpayer's qualified capital costs with respect to a facility are, or will result, in compliance with applicable EPA regulations, has been received, then the taxpayer shall be allowed the credit without obtaining certification from the CARB, unless CARB demonstrates that the fuel produced does not meet CARB regulations.

(3) "Facility" means a small refiner's petroleum refinery located in the State of California that has incurred qualified capital costs to produce ~~ultra-low~~ *ultra low* sulfur diesel fuel.

(4) "Applicable EPA regulations" means the Highway Diesel Fuel Sulfur Control Requirements of the Environmental Protection Agency.

(5) "Applicable CARB regulations" means the Vehicular Diesel Fuel Sulfur Control Requirements of the California Air Resources Board (CARB) under ~~Resolution 03-17~~ *Section 2281 of Article 2 of Chapter 5 of Division 3 of Title 13 of the California Code of Regulations.*

1 (6) “Applicable period” means, with respect to any facility, the
2 period beginning on January 1, 2004, and ending on May 31,
3 2007.

4 (7) ~~“Ultra-low~~ “*Ultra low* sulfur diesel fuel” means both of the
5 following:

6 (A) Diesel fuel with a sulfur content of 15 parts per million or
7 less.

8 (B) (i) Subject to clause (ii), either of the following:

9 (I) Vehicular diesel fuel produced and sold by a small refiner
10 on or after June 1, 2006.

11 (II) Vehicular diesel fuel produced and sold by the small
12 refiner before June 1, 2006, that the small refiner specifically
13 identifies and supports through internal test reports as meeting
14 applicable CARB regulations.

15 (ii) For purposes of this section, it is rebuttably presumed that
16 the fuel described in clause (i) is ~~ultra-low~~ *ultra low* sulfur diesel
17 fuel. The California Air Resources Board may rebut this
18 presumption by demonstrating that the fuel does not comply with
19 applicable CARB regulations.

20 (8) “Barrels per stream day” means the maximum number of
21 barrels of input that a distillation facility can process within a
22 24-hour period when running at full capacity under optimal crude
23 and product slate conditions with no allowance for downtime.

24 (d) For purposes of this section, if a credit is determined under
25 this section for any expenditure with respect to any property, the
26 increase in basis of that property that would (but for this
27 subdivision) result from that expenditure shall be reduced by the
28 amount of the credit so determined.

29 (e) No deduction shall be allowed for that portion of the
30 expenses otherwise allowable as a deduction for the taxable year
31 which is equal to the amount of the credit determined for the
32 taxable year under this section.

33 (f) In the case where the credit allowed by this section exceeds
34 the “tax,” the excess may be carried over to reduce the “tax” in
35 the following year, and the ~~six~~ 10 succeeding years if necessary
36 until the credit is exhausted.

37 (g) If a small refiner that claims a credit under this section
38 sells, transfers, or otherwise disposes of, either directly or
39 indirectly, a facility within five years of the taxable year during
40 which it first claimed the credit, there shall be added to the “tax”

1 of the small refiner during the taxable year of sale, transfer, or
2 disposition an amount equal to the total credit claimed multiplied
3 by a fraction, the numerator of which is the remaining term of
4 five years and the denominator of which is 5.

5 (h) This section shall remain in effect only until January 1,
6 ~~2013~~ 2018, and as of that date is repealed.

7 SEC. 53. Section 23701s of the Revenue and Taxation Code
8 is amended to read:

9 23701s. (a) An employee-funded pension trust described in
10 Section 501(c)(18) of the Internal Revenue Code, except as
11 otherwise provided.

12 (b) The last sentence in Section 501(c)(18) of the Internal
13 Revenue Code, relating to excess contributions under Section
14 4979, shall not apply.

15 SEC. 54. Section 23701w of the Revenue and Taxation Code
16 is amended to read:

17 23701w. A veteran's organization, as defined by Section
18 501(c)(19) of the Internal Revenue Code.

19 SEC. 55. Section 23703.5 of the Revenue and Taxation Code
20 is amended to read:

21 23703.5. Section 501(p) of the Internal Revenue Code,
22 relating to suspension of tax-exempt status of terrorist
23 organizations, shall apply, except as otherwise provided:

24 (a) References to Section 501(a) of the Internal Revenue Code
25 shall be modified to refer to Section 23701.

26 (b) Section 501(p)(4) of the Internal Revenue Code is
27 modified by substituting the phrase "under Part 10 (commencing
28 with Section 17001) and this part" for the phrase "under any
29 provision of this title, including ~~Section~~ sections 170, 545(b)(2),
30 556(b)(2), 642(c), 2055, 2106(a)(2), and 2522" contained therein.

31 (c) This section shall apply only during the period described in
32 Section 501(p)(3) of the Internal Revenue Code that the federal
33 tax exemption of the organization described in Section 501(p)(2)
34 of the Internal Revenue Code is suspended for federal income tax
35 purposes under Section 501(p)(1) of the Internal Revenue Code.

36 (d) Section 501(p)(5) of the Internal Revenue Code shall not
37 apply and in lieu thereof, notwithstanding any other provision of
38 law, no organization or other person may challenge a suspension
39 under this section, a designation or identification described in
40 Section 501(p)(2) of the Internal Revenue Code, the period of

suspension described in Section 501(p)(3) of the Internal Revenue Code, or a denial of a deduction under Section 501(p)(4) of the Internal Revenue Code as modified in subdivision (b) in any administrative or judicial proceeding relating to the California tax liability of the organization or other person.

(e) (1) Credit or refund (with interest) with respect to an overpayment shall be made if all of the following apply with respect to that overpayment:

(A) The tax exemption of any organization described in Section 501(p)(2) of the Internal Revenue Code is suspended under this section.

(B) Each designation and identification described in Section 501(p)(2) of the Internal Revenue Code which has been made with respect to that organization is determined to be erroneous under Section 501(p)(6) of the Internal Revenue Code for federal income tax purposes.

(C) The erroneous designations and identifications result in an overpayment of income tax for any taxable year by that organization.

(2) If the credit or refund of any overpayment of tax described in subparagraph (C) of paragraph (1) is prevented at any time by the operation of any law or rule of law (including res judicata), the credit or refund may nevertheless be allowed or made if the claim therefor is filed before the close of the one-year period beginning on the date of the last determination described in subparagraph (B) of paragraph (1).

(f) This section shall apply to designations made before, on, or after November 11, 2003.

SEC. 56. Section 23705 of the Revenue and Taxation Code is amended to read:

23705. (a) (1) An organization described in Section 23701i (voluntary employee's beneficiary associations) or 23701q (qualified group legal service plans) which is part of a plan of an employer shall not be exempt from tax under Section 23701, unless that plan meets the requirements of Section 505(b) of the Internal Revenue Code.

(2) Paragraph (1) shall not apply to any organization described in Section 505(a)(2) of the Internal Revenue Code.

1 (b) A copy of any notice filed with the Secretary of the
2 Treasury, pursuant to Section 505(c) of the Internal Revenue
3 Code, relating to application for tax-exempt status, shall be filed
4 at the same time and in the same manner with the Franchise Tax
5 Board.

6 SEC. 57. Section 23711 of the Revenue and Taxation Code is
7 amended to read:

8 23711. Section 529 of the Internal Revenue Code, relating to
9 qualified state tuition programs, shall apply, except as otherwise
10 provided.

11 (a) Section 529(a) of the Internal Revenue Code is modified as
12 follows:

13 (1) By substituting the phrase “under Part 10 (commencing
14 with Section 17001) and this part” in lieu of the phrase “under
15 this subtitle.”

16 (2) By substituting “Article 2 (commencing with Section
17 23731)” in lieu of “section 511.”

18 (b) A copy of the report required to be filed with the Secretary
19 of the Treasury under Section 529(d) of the Internal Revenue
20 Code shall be filed with the Franchise Tax Board at the same
21 time and in the same manner as specified in that section.

22 SEC. 58. Section 23712 of the Revenue and Taxation Code is
23 amended to read:

24 23712. Section 530 of the Internal Revenue Code, relating to
25 Coverdell education savings accounts, shall apply, except as
26 otherwise provided.

27 (a) Section 530(a) of the Internal Revenue Code is modified as
28 follows:

29 (1) By substituting the phrase “under Part 10 (commencing
30 with Section 17001) and this part” in lieu of the phrase “under
31 this subtitle.”

32 (2) By substituting “Article 2 (commencing with Section
33 23731)” in lieu of “section 511.”

34 (b) For taxable years beginning before January 1, 2002,
35 Section 530(b)(1) of the Internal Revenue Code, relating to the
36 definition of education savings account, is modified to
37 additionally require that upon the date that the designated
38 beneficiary becomes 30 years of age, any balance to the credit of
39 the beneficiary shall be distributed within 30 days after the date
40 the beneficiary becomes 30 years of age to that beneficiary.

(c) Section 530(d) of the Internal Revenue Code is modified as follows:

(1) By substituting the phrase “under Part 10 (commencing with Section 17001) in the manner as provided in Section 72(b) of the Internal Revenue Code, as modified by Part 10” in lieu of the phrase “in the manner as provided in Section 72(b)” in Section 530(d)(1) of the Internal Revenue Code.

(2) (A) By substituting the phrase “tax imposed by Part 10 (commencing with Section 17001)” in lieu of the phrase “tax imposed by this chapter” in Section 530(d)(4)(A) of the Internal Revenue Code.

(B) By substituting the phrase “increased by 2 ½ percent” in lieu of the phrase “increased by 10 percent” in Section 530(d)(4)(A) of the Internal Revenue Code.

(C) By substituting the phrase “shall be included in the contributor’s gross income under Part 10 (commencing with Section 17001) or this part” in lieu of the phrase “shall be included in gross income” in Section 530(d)(4)(C) of the Internal Revenue Code.

(D) For taxable years beginning before January 1, 2005:

(i) By additionally providing that Section 530(d)(4)(A) of the Internal Revenue Code, relating to additional tax for distributions not used for educational purposes, shall not apply if the payment or distribution is made on account of the attendance of the designated beneficiary at the United States Military Academy, the United States Naval Academy, the United States Air Force Academy, the United States Coast Guard Academy, or the United States Merchant Marine Academy, to the extent that the amount of the payment or distribution does not exceed the costs of advanced education (as defined by Section 2005(e)(3) of Title 10 of the United States Code, as in effect on November 11, 2003) attributable to that attendance.

(ii) The amendments made to this section by Section 12 of Chapter 552 of the Statutes of 2004 shall apply to taxable years beginning after December 31, 2002.

(d) For purposes of Part 10 (commencing with Section 17001) and this part, in the case of a custodial account treated as a trust by reason of Section 530(g) of the Internal Revenue Code, the custodian of that account shall be treated as the trustee thereof.

(e) A copy of the report, which is required to be filed with the Secretary of the Treasury under Section 530(h) of the Internal Revenue Code, shall be filed with the Franchise Tax Board at the same time and in the same manner as specified in that section.

SEC. 59. Section 24306 of the Revenue and Taxation Code is amended to read:

24306. (a) For purposes of this section, the following terms have the following meanings, as provided in the Golden State Scholarshare Trust Act (Article 19 (commencing with Section 69980) of Chapter 2 of Part 42 of the Education Code):

(1) “Beneficiary” has the meaning set forth in subdivision (c) of Section 69980 of the Education Code.

(2) “Benefit” has the meaning set forth in subdivision (d) of Section 69980 of the Education Code.

(3) “Participant” has the meaning set forth in subdivision (h) of Section 69980 of the Education Code.

(4) “Participation agreement” has the meaning set forth in subdivision (i) of Section 69980 of the Education Code.

(5) “Scholarshare trust” has the meaning set forth in subdivision (f) of Section 69980 of the Education Code.

(b) For taxable years beginning ~~before January 1, 2002, as on or after January 1, 1998, and before January 1, 2002, except as~~ otherwise provided in subdivision (c), gross income of a participant shall not include any of the following:

(1) Any earnings under a Scholarshare trust, or a participation agreement, as provided in Article 19 (commencing with Section 69980) of Chapter 2 of Part 42 of the Education Code.

(2) Contributions to the Scholarshare trust on behalf of a beneficiary shall not be includable as gross income of that beneficiary.

(c) For taxable years beginning *on or after January 1, 1998, and before January 1, 2002*:

(1) Any distribution under a Scholarshare trust participation agreement shall be includable in the gross income of the distributee in the manner as provided under Section 72 of the Internal Revenue Code, as modified by Section 24272.2, to the extent not excluded from gross income under any other provision of this part. For purposes of applying Section 72 of the Internal Revenue Code, the following apply:

1 (A) All Scholarshare trust accounts of which an individual is a
2 beneficiary shall be treated as one account, except as otherwise
3 provided.

4 (B) All distributions during a taxable year shall be treated as
5 one distribution.

6 (C) The value of the participation agreement, income on the
7 participation agreement, and investment in the participation
8 agreement shall be computed as of the close of the calendar year
9 in which the taxable year begins.

10 (2) A contribution by a for-profit or nonprofit entity, or by a
11 state or local government agency, for the benefit of an owner or
12 employee of that entity or a beneficiary whom the owner or
13 employee has the power to designate, including the owner or
14 employee's minor children, shall be included in the gross income
15 of that owner or employee in the year the contribution is made.

16 (3) For purposes of this subdivision, "distribution" includes
17 any benefit furnished to a beneficiary under a participation
18 agreement, as provided in Article 19 (commencing with Section
19 69980) of Chapter 2 of Part 42 of the Education Code.

20 (4) (A) Paragraph (1) shall not apply to that portion of any
21 distribution that, within 60 days of distribution, is transferred to
22 the credit of another beneficiary under the Scholarshare trust who
23 is a "member of the family," as that term is used in Section
24 529(e)(2) of the Internal Revenue Code, as amended by Section
25 211 of the Taxpayer Relief Act of 1997 (Public Law 105-34), of
26 the former beneficiary of that Scholarshare trust.

27 (B) Any change in the beneficiary of an interest in the
28 Scholarshare trust shall not be treated as a distribution for
29 purposes of paragraph (1) if the new beneficiary is a "member of
30 the family," as that term is used in Section 2032A(e)(2) of the
31 Internal Revenue Code, of the former beneficiary of that
32 Scholarshare trust.

33 (d) For taxable years beginning on or after January 1, 2002,
34 Sections 529(c) and 529(e) of the Internal Revenue Code shall
35 apply except as otherwise provided in Part 10 (commencing with
36 Section 17001) and this part.

37 SEC. 60. Section 24349 of the Revenue and Taxation Code is
38 amended to read:

1 24349. (a) There shall be allowed as a depreciation deduction
2 a reasonable allowance for the exhaustion, wear and tear
3 (including a reasonable allowance for obsolescence)—

4 (1) Of property used in the trade or business; or

5 (2) Of property held for the production of income.

6 (b) Except as otherwise provided in subdivision (c), for
7 taxable years ending after December 31, 1958, the term
8 “reasonable allowance” as used in subdivision (a) shall include,
9 but shall not be limited to, an allowance computed in accordance
10 with regulations prescribed by the Franchise Tax Board, under
11 any of the following methods:

12 (1) The straight-line method.

13 (2) The declining balance method, using a rate not exceeding
14 twice the rate that would have been used had the annual
15 allowance been computed under the method described in
16 paragraph (1).

17 (3) The sum of the years-digits method.

18 (4) Any other consistent method productive of an annual
19 allowance that, when added to all allowances for the period
20 commencing with the taxpayer’s use of the property and
21 including the taxable year, does not, during the first two-thirds of
22 the useful life of the property, exceed the total of those
23 allowances that would have been used had those allowances been
24 computed under the method described in paragraph (2).

25 Nothing in this subdivision shall be construed to limit or
26 reduce an allowance otherwise allowable under subdivision (a).

27 (c) Any grapevine replaced in a vineyard in California in a
28 taxable year beginning on or after January 1, 1992, as a direct
29 result of a phylloxera infestation in that vineyard, and any
30 grapevine replaced in a vineyard in California in a taxable year
31 beginning on or after January 1, 1997, as a direct result of
32 Pierce’s Disease in that vineyard, shall have a useful life of five
33 years, except that it shall have a class life of 10 years for
34 purposes of depreciation under Section 168(g)(2) of the Internal
35 Revenue Code where the taxpayer has made an election under
36 Section 263A(d)(3) of the Internal Revenue Code not to
37 capitalize costs of the infested vineyard. Every taxpayer claiming
38 a deduction under this section with respect to a grapevine as
39 described in this subdivision shall obtain a written certification
40 from an independent state-certified integrated pest management

1 adviser, or a state agricultural commissioner or adviser, that
2 specifies that the replanting was necessary to restore a vineyard
3 infested with phylloxera or Pierce's Disease. The taxpayer shall
4 retain the certification for future audit purposes.

5 (d) For purposes of this part, the deduction for property leased
6 to governments and other tax-exempt entities, as defined in
7 Section 168(h) of the Internal Revenue Code, shall be limited to
8 the amount determined under Section 168(g) of the Internal
9 Revenue Code, relating to alternative depreciation system for
10 certain property.

11 (e) (1) In the case of any building erected or improvements
12 made on leased property, if the building or improvement is
13 property to which this section applies, the depreciation deduction
14 shall be determined under the provisions of this section.

15 (2) An improvement shall be treated for purposes of
16 determining gain or loss under this part as disposed of by the
17 lessor when so disposed of or abandoned if both of the following
18 occur:

19 (A) The improvement is made by the lessor of leased property
20 for the lessee of that property.

21 (B) The improvement is irrevocably disposed of or abandoned
22 by the lessor at the termination of the lease by the lessee.

23 This subdivision shall not apply to any property to which
24 Section 168 of the Internal Revenue Code does not apply for
25 federal purposes by reason of Section 168(f) of the Internal
26 Revenue Code. Any election made under Section 168(f)(1) of the
27 Internal Revenue Code for federal purposes with respect to that
28 property shall be treated as a binding election for state purposes
29 under this subdivision with respect to that same property and no
30 separate election under subdivision (e) of Section 23051.5 with
31 respect to that property shall be allowed.

32 (3) (A) In determining a lease term, both of the following
33 shall apply:

34 (i) There shall be taken into account options to renew.

35 (ii) Two or more successive leases which are part of the same
36 transaction (or a series of related transactions) with respect to the
37 same or substantially similar property shall be treated as one
38 lease.

39 (B) For purposes of clause (i) of subparagraph (A), in the case
40 of nonresidential real property or residential rental property, there

1 shall not be taken into account any option to renew at fair market
2 value determined at the time of renewal.

3 (f) (1) Section 167(g) of the Internal Revenue Code, relating
4 to depreciation under income forecast method, shall apply except
5 as otherwise provided.

6 (2) Section 167(g)(2)(C) of the Internal Revenue Code is
7 modified by substituting “Section 19521” in lieu of “Section
8 460(b)(7)” of the Internal Revenue Code.

9 (3) Section 167(g)(5)(D) of the Internal Revenue Code is
10 modified by substituting “Part 10.2 (commencing with Section
11 18401) (other than Article 2 (commencing with Section 19021)
12 and Sections 19142 to 19150, inclusive)” in lieu of “Subtitle F
13 (other than Sections 6654 and 6655).”

14 (4) Section 167(g)(5)(E) of the Internal Revenue ~~Code Code~~,
15 *relating to treatment of distribution costs*, shall not apply.

16 (5) Section 167(g)(7) of the Internal Revenue ~~Code Code~~,
17 *relating to treatment of participations and residuals*, shall not
18 apply.

19 SEC. 61. Section 24355.3 is added to the Revenue and
20 Taxation Code, to read:

21 24355.3. For purposes of computing the depreciation
22 deduction pursuant to Section 24349, the useful life of any motor
23 sports entertainment ~~complex complex~~, as defined in Section
24 168(i)(15) of the Internal Revenue ~~Code Code~~, shall be seven
25 years.

26 SEC. 61.5. Section 24355.4 is added to the Revenue and
27 Taxation Code, to read:

28 24355.4. For purposes of computing the depreciation
29 deduction pursuant to Section 24349, the useful life of any Alaska
30 natural gas pipeline, as defined in Section 168(i)(16) of the
31 Internal Revenue Code, shall be seven years.

32 SEC. 62. Section 24356.4 is added to the Revenue and
33 Taxation Code, to read:

34 24356.4. (a) ~~A~~For any taxable year, which includes part of
35 the “applicable period,” as defined in paragraph (6) of
36 subdivision (c) of Section 23662, a small refiner (as defined in
37 Section 23662) may elect to treat 75 percent of qualified capital
38 costs (as defined in paragraph (2) of subdivision (c) of Section
39 23662) ~~for items that are placed in service paid or incurred by~~
40 the taxpayer during the taxable year as expenses that are not

1 chargeable to a capital account. Any cost so treated shall be
2 allowed as a deduction for the taxable year in which paid or
3 incurred.

4 (b) (1) For purposes of this part, the basis of any property shall
5 be reduced by the portion of the cost of that property taken into
6 account under subdivision (a).

7 (2) For purposes of Section 1245 of the Internal Revenue
8 Code, and corresponding section of this code, the amount of the
9 deduction allowable under subdivision (a) with respect to any
10 property which is of a character subject to the allowance for
11 depreciation shall be treated as a deduction allowed for
12 depreciation under Section 167 of the Internal Revenue Code, or
13 the corresponding section of this code.

14 (c) This section is repealed on January 1, 2009.

15 SEC. 63. Section 24356.5 of the Revenue and Taxation Code
16 is repealed.

17 SEC. 64. Section 24369.4 of the Revenue and Taxation Code
18 is amended to read:

19 24369.4. (a) Section 198 of the Internal Revenue Code,
20 relating to expensing of environmental remediation costs, shall
21 apply, except as otherwise provided.

22 (b) Section 198(b)(2) is modified to refer to Sections 24349 to
23 24355, inclusive, in lieu of Section 167 of the Internal Revenue
24 Code.

25 (c) Section 198(f) is modified to refer to Section 24442 in lieu
26 of Section 280B of the Internal Revenue Code.

27 (d) For expenditures paid or incurred before January 1, 2004,
28 each of the following shall apply:

29 (1) If a taxpayer has, at any time, made an election for federal
30 purposes under Section 198(a) of the Internal Revenue Code to
31 have Section 198 of the Internal Revenue Code apply to a
32 qualified environmental remediation expenditure, Section 198 of
33 the Internal Revenue Code shall apply to that qualified
34 environmental remediation expenditure for state purposes, a
35 separate election for state purposes shall not be allowed under
36 paragraph (3) of subdivision (e) of Section 23051.5, and the
37 federal election shall be binding for purposes of this part.

38 (2) If a taxpayer fails to make an election for federal purposes
39 under Section 198(a) of the Internal Revenue Code to have
40 Section 198 of the Internal Revenue Code apply to a qualified

1 environmental remediation expenditure, an election under
2 Section 198(a) of the Internal Revenue Code shall not be allowed
3 for state purposes, Section 198 of the Internal Revenue Code
4 shall not apply to that qualified environmental remediation
5 expenditure for state purposes, and a separate election for state
6 purposes shall not be allowed under paragraph (3) of subdivision
7 (e) of Section 23051.5.

8 (e) No inference as to the proper treatment for purposes of this
9 part of qualified environmental remediation expenditures for
10 periods before the enactment of this section shall be made.

11 (f) Section 198(h) of the Internal Revenue ~~Code~~ *Code, relating*
12 *to termination*, shall not apply.

13 (g) Section 198 of the Internal Revenue ~~Code~~ *Code, relating*
14 *to expensing of environmental remediation costs*, shall not apply
15 to expenditures paid or incurred after December 31, 2003.

16 SEC. 65. Section 24406.6 is added to the Revenue and
17 Taxation Code, to read:

18 24406.6. For purposes of Section ~~24373.5~~ 24373.5, and
19 Sections 24404 to 24406.5, inclusive, net earnings shall not be
20 reduced by amounts paid during the year as dividends on capital
21 stock or other proprietary capital interests of the organization to
22 the extent that the articles of incorporation, bylaws of the
23 organization, or other contract with patrons provide that those
24 dividends are in addition to amounts otherwise payable to patrons
25 that are derived from business done for or with patrons during the
26 taxable year.

27 SEC. 66. Section 24407 of the Revenue and Taxation Code is
28 amended to read:

29 24407. (a) The organizational expenditures of a corporation
30 may, at the election of the corporation (made in accordance with
31 regulations prescribed by the Franchise Tax Board), be treated as
32 deferred expenses. In computing net income, the deferred
33 expenses *remaining, if any, after the application of subdivision*
34 *(b)* shall be allowed as a deduction ratably over that period of not
35 less than ~~60~~ 180 months as may be selected by the corporation
36 (beginning with the month in which the corporation begins
37 business).

38 (b) (1) *The corporation shall be allowed a deduction for the*
39 *deferred expenses under subdivision (a) in an amount equal to*
40 *the lesser of either of the following:*

1 (A) The amount of organizational expenditures of the taxpayer
2 that are treated as deferred expenses under subdivision (a).

3 (B) Five thousand dollars (\$5,000), reduced, but not below
4 zero, by an amount equal to the difference between the amount of
5 the taxpayer's organizational expenditures treated as deferred
6 expenses under subdivision (a) and fifty thousand dollars
7 (\$50,000).

8 (2) The deduction under paragraph (1) shall be allowed in the
9 taxable year in which the first month of the period specified in
10 subdivision (a) occurs.

11 (c) The amendments made to this section by the act adding this
12 subdivision shall apply to amounts paid or incurred on or after
13 January 1, 2005.

14 ~~SEC. 66. Section 24407 of the Revenue and Taxation Code is~~
15 ~~amended to read:~~

16 ~~24407. If a corporation elects the application of this section~~
17 ~~(in accordance with regulations prescribed by the Franchise Tax~~
18 ~~Board) with respect to any organizational expenditures, the~~
19 ~~corporation shall be allowed a deduction for the taxable year in~~
20 ~~which the corporation begins business in an amount equal to~~
21 ~~either the amount of organizational expenditures with respect to~~
22 ~~the taxpayer or five thousand dollars (\$5,000), reduced (but not~~
23 ~~to below zero) by the amount by which those organizational~~
24 ~~expenditures exceed fifty thousand dollars (\$50,000), whichever~~
25 ~~is less. The remainder of those organizational expenditures shall~~
26 ~~be allowed as a deduction ratably over the 180-month period~~
27 ~~beginning with the month in which the corporation begins~~
28 ~~business.~~

29 SEC. 67. Section 24601 of the Revenue and Taxation Code is
30 amended to read:

31 24601. (a) Subchapter D of Chapter 1 of Subtitle A of the
32 Internal Revenue Code, relating to deferred compensation, etc.,
33 shall apply, except as otherwise provided.

34 (b) Notwithstanding the date specified in paragraph (1) of
35 subdivision (a) of Section 23051.5, Part I of Subchapter D of
36 Chapter 1 of Subtitle A of the Internal Revenue Code, relating to
37 pension, profitsharing, stock bonus plans, etc., shall apply, except
38 as otherwise provided, without regard to taxable year to the same
39 extent as applicable for federal income tax purposes.

SEC. 68. Section 24654 of the Revenue and Taxation Code is amended to read:

24654. (a) Section 448 of the Internal Revenue Code, relating to limitation on use of cash method of accounting, shall apply, except as otherwise provided.

(b) For purposes of applying Section 448 of the Internal Revenue Code, Sections 801(d)(2), 801(d)(3), and 801(d)(5) of the Tax Reform Act of 1986 (Public Law 99-514), as modified by Section 1008(a) of Public Law 100-647, shall apply to each taxable year beginning on or after January 1, 1987.

SEC. 69. Section 24661.5 of the Revenue and Taxation Code is amended to read:

24661.5. Section 451(e)(3) of the Internal Revenue Code, relating to special election ~~rule~~ *rule*, is modified by substituting the phrase “subdivision (b) of Section 24949.1” in lieu of the phrase “section 1033(e)(2)” contained therein.

SEC. 70. Section 24661.6 is added to the Revenue and Taxation Code, to read:

24661.6. Section 451(i) of the Internal Revenue Code, relating to special rule for sales or dispositions to implement Federal Energy Regulatory Commission or state electric restructuring policy, shall not apply.

SEC. 71. Section 24694 is added to the Revenue and Taxation Code, to read:

24694. Section 470 of the Internal Revenue Code, relating to limitation on deductions allocable to property used by governments or other tax-exempt entities, shall apply, except as otherwise provided.

SEC. 72. Section 24831.6 is added to the Revenue and Taxation Code, to read:

24831.6. Section 613A(c)(6)(H) of the Internal Revenue Code, relating to temporary suspension of taxable income limit with respect to marginal production, shall not apply.

SEC. 73. Section 24872 of the Revenue and Taxation Code is amended to read:

24872. (a) A real estate investment trust shall be deemed to have satisfied the distribution requirements of Section 857(a)(1) of the Internal Revenue Code for purposes of this part if it satisfies the distribution requirements of Section 857(a)(1) of the Internal Revenue Code for federal purposes.

1 (b) (1) Section 857(b)(1) of the Internal Revenue Code,
2 relating to imposition of tax on real estate investment trusts, shall
3 not apply.

4 (2) Every real estate investment trust shall be subject to the
5 taxes imposed under Chapter 2 (commencing with Section
6 23101) and Chapter 3 (commencing with Section 23501), except
7 that its “net income” shall be equal to its “real estate investment
8 trust income,” as defined in subdivision (c).

9 (c) “Real estate investment trust income” means real estate
10 investment company taxable income, as defined in Section
11 857(b)(2) of the Internal Revenue Code, modified as follows:

12 (1) In lieu of Section 857(b)(2)(A) of the Internal Revenue
13 Code, relating to special deductions for corporations, no
14 deduction shall be allowed under Section 24402.

15 (2) Section 857(b)(2)(D) of the Internal Revenue Code,
16 relating to an exclusion for an amount equal to the net income
17 from foreclosure property, shall not apply.

18 (3) Section 857(b)(2)(E) of the Internal Revenue Code,
19 relating to a deduction for an amount equal to the tax imposed in
20 the case of failure to meet certain requirements for the taxable
21 year, shall not apply.

22 (4) Section 857(b)(2)(F) of the Internal Revenue Code,
23 relating to an exclusion for an amount equal to any net income
24 derived from prohibited transactions, shall not apply.

25 (d) Section 857(b)(3) of the Internal Revenue Code, relating to
26 an alternative tax in case of capital gains, shall not apply.

27 (e) Section 857(b)(4)(A) of the Internal Revenue Code,
28 relating to the imposition of tax on income from foreclosure
29 property, shall not apply.

30 (f) Section 857(b)(5) of the Internal Revenue Code, relating to
31 the imposition of tax in case of failure to meet certain
32 requirements, shall not apply.

33 (g) Section 857(b)(6)(A) of the Internal Revenue Code,
34 relating to the imposition of tax on income from prohibited
35 transactions, shall not apply.

36 (h) Section 857(b)(7) of the Internal Revenue Code, relating to
37 income from redetermined rents, redetermined deductions, and
38 excess interest, shall not apply.

39 (i) Section 857(c) of the Internal Revenue Code, relating to
40 restrictions applicable to dividends received from real estate

1 investment trusts, is modified to refer to Sections 24402, 24406,
2 24410, and 25106, in lieu of Section 243 of the Internal Revenue
3 Code.

4 (j) The amendments to this section by Chapter 878 of the
5 Statutes of 1993 are clarifications of legislative intent and shall
6 apply to taxable years beginning on or after January 1, 1987.

7 SEC. 74. Section 24949.1 of the Revenue and Taxation Code
8 is amended to read:

9 24949.1. (a) For purposes of this part, the sale or exchange of
10 livestock (other than poultry) held by a taxpayer for draft,
11 breeding, or dairy purposes in excess of the number the taxpayer
12 would sell if he or she followed his or her usual business
13 practices shall be treated as an involuntary conversion to which
14 Sections 24943 to 24949, inclusive, apply if the livestock are
15 sold or exchanged by the taxpayer solely on account of drought,
16 flood, or other weather-related conditions.

17 (b) (1) In the case of drought, flood, or other weather-related
18 conditions described in subdivision (a) that result in the area
19 being designated as eligible for assistance by the federal
20 government, subdivision (b) of Section 24944 shall be applied
21 with respect to any converted property by substituting “four
22 years” for “two years.”

23 (2) The Franchise Tax Board may extend the period for
24 replacement under Sections 24943 to 24949, inclusive (after the
25 application of ~~paragraph (1))~~ *paragraph (1)*), for the additional
26 time as the Franchise Tax Board determines appropriate if the
27 weather-related conditions that resulted in the application of
28 paragraph (1) continue for more than three years.

29 SEC. 75. Section 24949.3 of the Revenue and Taxation Code
30 is amended to read:

31 24949.3. For purposes of Sections 24943 through 24946, if,
32 because of drought, flood, other weather-related conditions, or
33 soil contamination or other environmental contamination, it is not
34 feasible for the taxpayer to reinvest the proceeds from
35 compulsorily or involuntarily converted livestock in property
36 similar or related in use to the livestock so converted, other
37 property (including real property in the case of soil
38 contamination or other environmental contamination) used for
39 farming purposes shall be treated as property similar or related in
40 service or use to the livestock so converted.

1 SEC. 76. Sections 411 to 418, inclusive, of the Job Creation
2 and Worker Assistance Act of 2002 (Subtitle B of Title IV of
3 Public Law 107-147) and Sections 401 to 408, inclusive, of the
4 Working Families Tax Relief Act of 2004 (Public Law 108-311)
5 enacted numerous technical corrections to provisions of the
6 Internal Revenue Code, including technical corrections relating
7 to the Medicare Prescription Drug, Improvement, and
8 Modernization Act of 2003 (Public Law 108-173), the Jobs and
9 Growth Tax Relief Reconciliation Act of 2003 (Public Law
10 108-27), the Job Creation and Worker Assistance Act of 2002
11 (Public Law 107-147), the Economic Growth and Tax Relief
12 Reconciliation Act of 2001 (Public Law 107-16), the Community
13 Renewal Tax Relief Act of 2000 as part of the Consolidated
14 Appropriations Act, 2001 (Public Law 106-554), the Tax Relief
15 Extension Act of 1999 as part of the Ticket to Work and Work
16 Incentives Improvement Act of 1999 (Public Law 106-170), the
17 Taxpayer Relief Act of 1997 (Public Law 105-34), the Balanced
18 Budget Act of 1997 (Public Law 105-33), and the Small Business
19 Job Protection Act of 1996 (Public Law 104-188), some of which
20 are incorporated by reference into Part 10 (commencing with
21 Section 17001), Part 10.2 (commencing with Section 18401), and
22 Part 11 (commencing with Section 23001) of Division 2 of the
23 Revenue and Taxation Code. Unless otherwise specifically
24 provided, the technical corrections described in the preceding
25 sentence, to the extent that they correct provisions that are
26 incorporated by specific reference into the Revenue and Taxation
27 Code, are declaratory of existing law and shall be applied in the
28 same manner and for the same periods as specified in the Job
29 Creation and Worker Assistance Act of 2002 (Subtitle B of Title
30 IV of Public Law 107-147) and the Working Families Tax Relief
31 Act of 2004 (Public Law 108-311), or if later, the specified date
32 of incorporation.

33 SEC. 77. The amendments made by the enactment of this act
34 that incorporate by reference the amendments made by Section
35 1201 of the Medicare Prescription Drug, Improvement, and
36 Modernization Act of 2003 (Public Law 108-173), which added
37 Section 223 of the Internal Revenue Code to Part VII of
38 Subchapter B of Chapter 1 of Subtitle A of the Internal Revenue
39 Code and made amendments to Sections 62, 106, 125, and 220 of
40 the Internal Revenue Code, shall apply to taxable years

1 beginning after December 31, 2003. The Legislature declares that
2 the amendments made by the enactment of this act and the
3 retroactive application ~~contained in the preceding sentence~~
4 *provided by the preceding sentence of this section* are necessary
5 for the public purpose of conforming state *income tax* law to the
6 addition of Section 223 of the Internal Revenue Code by Section
7 1201 of the Medicare Prescription Drug, Improvement, and
8 Modernization Act of 2003 (Public Law 108-173) and thereby
9 prevent undue hardship to taxpayers that would otherwise have
10 been subject to tax and penalties from health plan conversions
11 from Archer Medical Savings Accounts to Health Savings
12 Accounts under Sections 220 and 223 of the Internal Revenue
13 Code. ~~Notwithstanding any provision of law to the contrary, the~~
14 ~~statute of limitations for the filing of a claim for refund with~~
15 ~~respect to the retroactive application contained in the first~~
16 ~~sentence of this section shall not expire before April 15, 2010.~~
17 *Code. If a refund or credit of any overpayment of tax resulting*
18 *from the retroactive application provided by the first sentence of*
19 *this section is prevented at any time before the close of the*
20 *two-year period beginning on the effective date of the act adding*
21 *this section by the operation of any law or rule of law (including*
22 *res judicata), that refund or credit may nevertheless be made or*
23 *allowed if the claim therefor is filed before the close of that*
24 *period.*

25 SEC. 77.5. Section 44 of this bill incorporates amendments to
26 Section 19008 of the Revenue and Taxation Code proposed by
27 this bill and SB 157. It shall not become operative if (1) both bills
28 are enacted and become effective on or before January 1, 2006,
29 (2) each bill amends Section 19008 of the Revenue and Taxation
30 Code, and (3) this bill is enacted after SB 157.

31 SEC. 77.6. Section 2.5 of this bill incorporates amendments
32 to Section 17052.6 of the Revenue and Taxation Code proposed
33 by both this bill and AB 1766. It shall only become operative if
34 (1) both bills are enacted and become effective on or before
35 January 1, 2006, (2) each bill amends Section 17052.6 of the
36 Revenue and Taxation Code, and (3) this bill is enacted after AB
37 1766, in which case Section 2 of this bill shall not become
38 operative.

1 SEC. 78. This act provides for a tax levy within the meaning
2 of Article IV of the Constitution and shall go into immediate
3 effect.

O